The Province of Alberta

IN THE MATTER OF THE PUBLIC INQUIRIES ACT

—and—

IN THE MATTER OF a Commission, dated the 12th day of October, A.D. 1938, to inquire into matters connected with Petroleum and Petroleum Products

Commissioners:

The Honourable MR. JUSTICE McGILLIVRAY
(*Chairman*)

—and—

L. R. LIPSETT, ESQ.

Session:

CALGARY, Alberta June 12th, 1939.

VOLUME 75.

MR. FRAWLEY: Mr. Shaw has a statement to make.

MR. SHAW: If Your Lordship pleases, on Friday last the session concluded under circumstances in which I asked that I might have an opportunity, as it were, to circumscribe any inferences or suggestions which might be drawn from any statements made by Mr. Plotkins. I had a discussion with Mr. Frawley and subsequently with my client and I would like to say now, My Lord, as frankly and fully as I can that if, in the course of the evidence given before this Commission, Mr. Plotkins has made observations or any statements which either directly impute improper conduct or dishonesty or from which perhaps inferences may be drawn of improper conduct on the part of anyone and everyone then, Sir, I would like on his behalf, to wholly withdraw and retract any suggestions of that kind. As I conceive it, My Lord, the usefulness of Mr. Plotkins to this Commission consists in his ability and his specialized knowledge to present particular facts which may have a bearing on the points before this Commission and it is a matter of regret perhaps, and perhaps not wholly not understandable on his part, that he has been led into making these observations, I think it is unfortunate, and it is manifestly unfair to the people who have been affected by those observations and so I would like to make that complete and frank withdrawal of any improper and dishonest suggestions which may reflect upon the conduct of anyone.

MR. FRAWLEY: Well we were dealing, when Mr. Plotkins was in the box, we were dealing

MR. FRANKLIN: [illegible]

Mr. [illegible]

THE CHAIRMAN: [illegible]

[illegible] letter that the [illegible]

in which I asked that I might [illegible] the committee as in

part to [illegible] any [illegible] or suggestions which

might be drawn from my [illegible] to Mr. Franklin.

I had a discussion with Mr. [illegible] and subsequently

with my client and I would like [illegible], as

frankly and fairly as I can [illegible] the course of the

evidence given before this committee, Mr. [illegible] has

made observations or statements which [illegible]

[illegible] or [illegible] that

inferences may be drawn of improper conduct on the part of

[illegible] and [illegible] I would like [illegible]

to [illegible] any [illegible] of that

kind. [illegible]

Mr. Franklin to [illegible] Commission [illegible] his

and his [illegible]

which may have a bearing on the points before this

Commission [illegible]

perhaps you [illegible]

[illegible]

[illegible]

[illegible]

would like [illegible]

or any [illegible]

[illegible]

rather particularly, at least I had begun to deal with any imputations of personal dishonesty or anything of that sort which might affect Mr. Aberhart and I was beginning to discuss with Mr. Plotkins the letter which at his request I obtained from the Royalite Oil Company. I recollect that I had not completed that cross-examination when I think it was that Mr. Shaw intervened, or in any event I was interrupted in the course of that examination, and before Mr. Shaw concludes, if he sees fit, I think in addition to his general denial, that he should make specific reference to those people whom we know to have been connected, some very lightly and some only by implication indirectly and some more particularly by Mr. Plotkins, and I refer particularly to the witness Mr. Hill and to Mr. Aberhart.

MR. SHAW: If my learned friend wishes my observations specialized I have no objection to applying them to the gentlemen he suggests and I certainly want to take the opportunity, in the presence of Mr. Brownlee, to make them especially applicable to him. I do not want Mr. Brownlee to go away with any suggestion that for a single moment it is going to be suggested at any time that he has been guilty of any improper or dishonorable conduct during his capacity as premier of this province or at any other time.

MR. FRAWLEY: Perhaps about that, so that it will not be misunderstood, the reason I did not mention Mr. Brownlee a moment ago was because Mr. Shaw had dealt with him rather fully on Friday afternoon in the way of a retraction.

THE CHAIRMAN: Mr. Shaw, we are very pleased that you should make these statements which you have. As Mr. Frawley says he was about to cross-examine the witness Plotkins with regard to any suggestion or imputation that may have been made with reference to Premier Aberhart at the time that you will remember you intervened, to make the statement that you did on Friday. Now I just want to add to what I said on Friday and my fellow Commissioner agrees with what I now say. Since that time I have taken the opportunity to read the letter referred to and as a result of my reading of this letter from Mr. Le Sueur to Mr. McLeod, Exhibit "284", of which something was made, I must say that, aside from some observations with regard to what has been described in that letter as "The Social Credit System" which is irrelevant to this inquiry, I find nothing therein, even as I find nothing in the evidence as a whole, and as I have said I speak for the both of us, which in any wise would serve to reflect upon the honor, the honesty and the integrity of the Premier of this province. There is the statement that the Premier, - as one would expect of any Premier, - said that before any interests are adversely affected in Turner Valley, or elsewhore I gather, that those that will be affected will be given an opporunity of being heard, his only stipulation being that they act speedily in presenting their side of the case. To my mind it is not only not objectionable but exceedingly pleasing to know that any government would hear those who are to be greatly affected by their legislation before passing that legislation. I see nothing whatsoever in that letter which is not only fully capable of an innocent construction but which approaching it in an

intelligent and a fair fashion, can lead to any other construction. I may say that I am pleased that you have made your statements for another reason and that is that we think your client, with his specialized knowledge, can perhaps put before us, as well as anyone might, what

legislation he considers is working a hardship upon those who are interested in Turner Valley. It is wholly unnecessary to suggest that those who have the onerous duty of passing laws which they think will help their people, - there is no purpose to it, - to suggest that they are criminals unless it is possible to prove clearly that they are. If they were it might be of interest, but to voice suspicions and destroy reputations when there is nothing more to it, seems to us most objectionable procedure. Now we are very much interested in reporting on any legislation that can be shown to us to be adversely affecting Turner Valley. If we had no other authority it would seem to us that the Omnibus Clause to which you have before referred would be all sufficient. We are interested in exploring any avenue that will serve to throw light on the whole situation in Turner Valley, which in turn must affect prices with which we are particularly concerned. We think your client can be of assistance and under your guidance we hope he will be and we need not repeat that we wish to hear no more of the traducing of people, unless it can be shown that they are guilty of the act with which they are charged.

MR. FRAWLEY: Mr. Brownlee is here and desires to make a statement.

[illegible]

[illegible] tion [illegible]

[illegible]

[illegible]

duty of [illegible] think [illegible]

people, [illegible]

they are [illegible] rights [illegible]

[illegible]

but to [illegible]

ficers is [illegible]

objection [illegible]

[illegible]

adversely affecting [illegible]

It would now [illegible]

have before [illegible]

Independent [illegible]

[illegible]

unless in [illegible]

[illegible]

[illegible]

[illegible]

[illegible]

JOHN E. BROWNLEE, having been first duly sworn, said:-

THE WITNESS: My Lord and Mr. Commissioner, after hearing what Mr. Shaw said this morning it may be that what I had intended to say is somewhat now beside the point. I can only say that anything I have prepared, what I have prepared was prepared before I knew that any retraction had been made and without wishing to attach undue importance to the statements which were made by Mr. Plotkins, as particularly reported in Volume 69 of the proceedings, I feel that in fairness to the Commission as well as in justice to my former colleagues and also my friends in the province, that I cannot permit those statements to stand without a reply and for the purposes of clarity and conciseness I propose to deal with all the various allegations there given and I think probably I can best serve the Commission by simply reading what I have and then I will be glad to answer any questions if I have not made myself clear.

1. I refer to the evidence reported on pages 8247 to 8250 inclusive. I think this portion of the evidence can be fairly summarized as follows:- That the Dominion Government under the Premiership of the Right Honourable R. B. Bennett commenced "flirting with the idea of making a deal with one or more of the major oil companies to control the number of refineries which were considered at that time as too many" as well as the number of distributing points; that he approached the Imperial and British American Oil Companies with that purpose in mind; that he subsequently

called a conference of Provincial Premiers at which the subject was discussed; that considerable publicity resulted which was subsequently hushed up; that he intimated to the major oil companies that to avoid too great political repercussion they should buy up the smaller independent refineries; that an organization was formed in Chicago with Mr. Sackett at its head and that this organization did buy up the most of the independent oil refineries; that I particularly became very enthusiastic over the plan and proceeded to pass legislation and to inaugurate policies to put this plan into effect and that this had the result of restricting the right of distributing organizations to expand.

I feel that that is a fair summary of that part of the evidence.

The Right Honourable R. B. Bennett is most competent to speak for himself and requires no defence by me. Speaking for myself I wish to say positively and definitely that neither he nor any member of his Government ever suggested such a plan to me. It was never the subject of discussion between him and me. It was never a subject of discussion at a conference of Provincial Premiers. I would not wish to go so far as to swear that in some of the discussions at the Dominion-Provincial Conferences, for example with respect to highway development, the expansion of distributing facilities was never incidentally or even casually referred to although I have no recollection of even such a casual or incidental discussion.

I probably may interject here to say that the agendas, - that after each Dominion-Provincial Conference there was . made available to anyone who may now wish to inquire, not only the agendas of those conferences but also a precis following, outlining the discussions which took place so that anything I may say as to what took place at these Dominion-Provincial Conferences or any of them, can be verified by reference to those agendas and preces which were prepared following the Conference.

I repeat however that at no time was any plan for the curtailment of refinery facilities or wholesale or retail distributing agencies ever the subject of discussion between members of the Dominion Government and myself. I may add that I happened to meet Mr. M. A. McPherson, Attorney-General for Saskatchewan during the time of the Bennett regime and I showed him this evidence and he authorized me to associate him in this denial.

That is he also said there was never any such discussion either at the Conferences or with his government.

I never even heard of Mr. Sackett until some time after I had resigned from the Premiership and I will make a reference to that occasion later. Moreover it must be remembered that during the time I was Premier there was no over-development of manufacturing facilities in this Province, the only refineries at that time being the Imperial Refinery at Calgary

and three or four small refineries located at Coutts, Calgary and Edmonton. So far as this Province was concerned therefore there was not during that time the slightest concern about over-expansion of refinery facilities. I might add in passing that as late as 1934 I endeavoured to interest certain companies in the establishment of refineries in this Province.

Now I would like to interject this too, that a reference is made in that evidence to the fact that there was considerable publicity in the financial papers and that that publicity was in some way hushed up. I have tried to be a consistent and faithful reader of the most of the financial papers in Canada for many years past, as well as the leading financial papers in the United States, and I personally have never seen that publicity and would be very much interested if it were made available to me because I doubt if there was any such publicity at any time.

So far as I am concerned therefore there is no foundation in fact for the assertions made by Mr. Plotkins in this part of his evidence.

2. Restriction on expansion of distribution facilities. This is referred to on page 8249 of the evidence in the following words:

" Now I found at the time that that was the
"policy that the Premier himself had apparently
"initiated, but the members of the, even the
"Cabinet that I consulted at the time and private
"members of the Legislature did not know a thing
"about it. Now when that came about, the reason

"I came to that conclusion is this, when I was "faced with that particular few lines in the Fuel "Oil Tax Act which came out without any publicity, "without any discussion, in the House, it was "never brought before the House, I went to Edmonton "and I asked the different Departments how this "particular clause restricting the number of "service stations in the future had come about, "because there certainly was no bill about it, there "was certainly no discussion in the House about it, "and it could not very well be put in in the form "of a regulation because it would then have to go "before the House at the next session for certifica- "tion and approval and I was told by the Provincial "Secretary's Department at the time, either the "Deputy Minister or some of the other officials, "that it had just come about, no explanation. Mr. "Brownlee insisted and put it in here personally. "Now from that time on we began to be up against "trouble in our desires, and when I say "ours" I "mean our company's desires to expand our facilities "in a normal way."

That is the statement.

Now I think that a fair reading of that statement would lead to the clear inference that I put through some restriction which was not authorized by legislation and of which the Members of the Legislature were not aware. As a Judge of the Supreme Court, a former practicing lawyer, and a former Member of the Legislature, Mr. Chairman, you will fully appreciate -

(a) That any restriction or regulation not

authorized by legislation would be invalid and of no effect, and

(b) That an Act of the Legislature has to follow certain well defined procedure in the Legislature; and that regardless of suggestions made to the contrary there is a fair proportion of the Members who are keenly alive to any legislation introduced.

For the information of this Commission I should probably say that the first suggestion of licensing wholesale and retail distributors of gasoline is found in Chapter 44 of the Statutes of Alberta, 1932.

That was a revision of the Fuel Oil Tax Act. This Act was introduced in the Legislature as Bill 56, had its first reading on March 21st, its second reading on March 22nd, went before the Committee of the whole House on April 1st when progress was reported, went into Committee again on April 4th and was given its third reading on April 5th. Those dates, I may say, were prepared for me by Mr. Anderson as clerk of the House and I am speaking on his authority. This Bill was the result of certain discussions in the Legislature earlier in the Session with respect to the proper collection of the Fuel Oil Tax. It was suggested that we had not been sufficiently active and careful in the collection of that tax. It was felt that the payment of the tax was being evaded and the Department had had occasion to prosecute certain individuals for non-payment. The Government referred the matter to a committee consisting of Mr. James Thompson, the Provincial Auditor; Mr. Trow-

bridge, the Deputy Minister; and Mr. R. Andrew Smith, Legislative Counsel. As a result of their study two suggestions were made, first that inspectors should be put in the field to check up all distributing agencies, and secondly, that for the purpose of more completely identifying legitimate selling agencies all distributors should be required to take out a license. This latter provision was incorporated in the revision of the former Gasoline Tax Act of 1929, what had been known as The Gasoline Tax Act of 1929 as contained in said Chapter 44 of 1932, being the Act to Impose a Tax on Fuel Oil. Now a reading of this Act will show that in its origin the licensing system was not related to the restriction of distributing facilities at all but was devised solely as a means to enforce the payment of the tax. This is shown particularly by Sections 21 and 22 of the Act which restricted the right of the Minister to cancel or deny a license to infractions of the Act. There was not in this Act the slightest suggestion of curtailing distributing agencies for any other reason. I may say that I would venture the opinion that if the present officers of the Provincial Government who were then in office also and had charge of these licenses were called to this stand they would verify this statement that no instance can be found under that Act or the administration of that Act where a license was refused or denied or cancelled on any other ground than because of some record of non-payment of taxes.

By 1934 the question of the expansion of retail, but not wholesale, distributing

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stations and the possible effect of that expansion on the cost of gasoline had been raised in several of the Provinces and at least one of the Eastern Provinces, Nova Scotia, had taken steps to curtail this expansion. My recollection is that they passed an Act which had the effect of reducing the then present number, as well as curtailing the future extension of retail distributing agencies. The question, therefore, came before the Legislature on our own initiative and without any suggestion from outside sources. It was felt that it would not be wise to attempt to curtail existing facilities in fairness to those who had caused them to be created but that some regulation might be introduced with respect to new facilities, with the result that Bill No. 43 was introduced into the Legislature on March 22nd, 1934, was given its second reading on March 29th, went to the Committee of the whole House on April 4th when progress was reported, was again before the House on April 11th, that is the Committee of the whole House, was re-committed to the Committee of the whole House on April 13th and was not finally passed until April 16th. It will be seen that this Bill was on the order paper of the Legislature every day from March 22nd to April 16th and there was plenty of opportunity for discussion in the Legislature. This Bill provided that new applications for licenses as retail dealers,and we did not do anything about the wholesalers, might be referred by the Minister either to the Board of Public Utility Commissioners or to an advisory committee appointed under the Department of Trade and Industries Act. In actual

practice the references were made to the Board of Public Utility Commissioners. Now I doubt if Mr. Carpenter ever forgave us for putting that load upon him because it proved to be an onerous one but I think he would agree that never at any time was influence either directly or indirectly ever brought to bear upon him in any decision he made under that Act. This was the first and only Legislative or Governmental action taken during my term of office to restrict the expansion of retail distribution facilities and in view of the fact that it was before the House for twenty-five days, there can surely be no suggestion of concealment.

In this connection I should probably refer to the evidence on page 8277 which might leave the inference that this policy was actuated by the contract between Maple Leaf Petroleum Limited and the U. F. A. Central Co-operative Association Limited. I have only to point out that that contract was not made until after I had resigned from the Premiership and was not even contemplated at the time this legislation was passed. The U. F. A. Central Co-operative Association at that time had its contract with the Great West Distributors Ltd. and the legislation affected them as much as any other company or organization.

May I emphasize again that this legislation was passed on our own responsibility and without any suggestion from either the Dominion Government or the Governments of the other Provinces, although we looked to their experiences, that is the experiences of the other Provinces, and it is of course

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a matter of common knowledge that the present Government of Alberta has deemed it expedient to continue this policy by placing the supervision entirely within the Department of Trade and Industry. Lest this statement be misunderstood I should probably add that in any contact I have recently had with the Officials of the Department in this respect, I have no reason to question the good faith with which these officials are carrying on their duties.

3. Alleged restriction on drilling. At the top of page 8252 I find the following:

"but it had another big repercussion and that
"is Mr. Brownlee was then favourable to any action
"that might also rationalize the Turner Valley
"situation, and he proceeded to restrict drilling,
"to bring about conditions in Turner Valley that
"at least resulted in turning over the greater
"portion of the field to the Imperial Oil."

The reference there made is to the alleged negotiations with Premier Bennett above referred to.

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The only way in which the Government of Alberta could possibly affect drilling in the Turner Valley would be, first, by restrictive regulations in the Department of Lands and Mines, and secondly by policies of gas conservation in the Turner Valley.

With respect to the first, the Government of Alberta had nothing whatever to do with regulations affecting the Turner Valley Oil Field until after the transfer of the natural resources in 1930. Practically all of the existing leases in the Turner Valley had been granted by the Dominion Government prior to that date. It is a matter of simple record that practically no leases were granted in the Turner Valley by the Provincial Government, during our term of office. By the terms of transfer the Government of Alberta obligated itself not to interfere with contracts previously made by the Dominion Government excepting by general legislation or by general regulation. Prior to 1930 the question of gas conservation had become the subject of considerable discussion in the Province, although we were powerless to act ourselves and as a result of discussions between our Government and the then Liberal Government at Ottawa, a joint study had been made of the problem with such men as Mr. Camsell, C. C. Ross and Mr. Calder, and other officials of the Dominion Government assisting. Upon the completion of the transfer of the natural resources the Alberta Government enacted regulations - I may say in their study they were of course in touch with all the companies that were producing in Turner Valley.

(a) Restricting drilling to two hundred feet between wells and from the boundaries of the property. (This is a common restriction in many oil fields and so far as I know was not objected to in the Turner Valley).

(b) By restricting the output to twenty-five per cent of the normal flow.

That was for the purpose of gas conservation. Now I may say, too, that all of these regulations were regulations that had been advised by the Committee, the joint Committee of the Provincial and the Dominion Governments which I referred to before.

MR. COMMISSIONER LIPSETT: That (b) referred to gas only, I suppose?

A Yes. It was intended as a gas conservation policy. Of course the problem in Turner Valley in those days, I do not know what it is today, but in those days when the problem of conservation in Turner Valley came up, the difficulty was just to decide as to whether it was an oil field or a gas field. At that time there was undoubtedly a very great wastage of gas, and particularly the men I am going to refer to later came to the conclusion that at that time at least it had to be regarded as a gas field rather than as an oil field. The whole foundation, I think, you will find, if you refer to the report I am about to mention, if you refer to that I think you will find the whole foundation of that report was on the theory it had to be regarded at that time as a gas field and not as an oil field. That was the opinion of Dr. Wallace who was at the head of the Commission.

A regulation was also enacted restricting the size of new leases to a minimum of one hundred and sixty acres

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instead of forty acres as was previously the case. As practically no new leases were granted in the Turner Valley this restriction had no effect upon that field. These, as a matter of record, were the only new regulations made by us under The Lands and Mines Act and they had no effect of materially restricting drilling.

The question of conservation continued to be a moot question in the Province, and I may quite frankly say there was dissatisfaction with the regulations restricting the normal flow to 25%, with the result that the Government engaged Mr. Fisher, the well known gas expert, to make a study of the field, and subsequently appointed a commission unddr the chairmanship of Dr. Wallace, President of the University, assisted by Mr. Carpenter, Chairman of the Public Utility Board, and Mr. McLeish of the Department of Natural Resources at Ottawa, to make a study of the whole situation. This commission continued to have the advice of Mr. Fisher, and also obtained the services of, I think I am right in this, Mr. Frawley, it was Mr. Brewster.

MR. FRAWLEY: Yes, Mr. Brewster.

A Of Bradford, Pennsylvania.

MR. FRAWLEY: Yes, that is right.

A Mr. Brewster, of Bradford, Pennsylvania. At the time I dictated this I was not sure of the name, and I had to look it up afterwards. Mr. Brewster of Bradford, Pennsylvania, a well known oil and gas authority. Following the work of this commission, the whole matter came before the Legislature in 1932, was thoroughly discussed before the Committee of the

whole House, and as a matter of fact I think the larger term of that Session was devoted to discussions before the committee of the whole House on this question of oil and gas conservation, and the Oil Industry were givem ample opportunity to make representations. By widening the restriction to 40% of the open flow, complete agreement was reached with those appearing for the producing companies and the Act for the Conservation of the Gas Resources of the Turner Valley, being Chapter 6 of the Statutes of Alberta, 1934, was subsequently passed with very little discussion in the House, and with almost, if not entire, unanimity in the House. As a matter of fact I am of the opinion the Act was passed unanimously.

MR. FRAWLEY: I think that must be 1932, that Chapter 6.

A That is true. That is a mis-statement here. It was 1932.

MR. FRAWLEY: Yes, Chapter 6 of 1932?

A Yes, that is just a typographical error. It was 1932. Immediately following the work of the Commission of which Dr. Wallace was the head. As no other action of any kind was taken with respect to the Turner Valley by the Government during my term of ooffice it is difficult to understand how it can be said that the Government either restricted drilling or that the policies of the Government resulted in turning the field over to Imperial Oil. In fact it is clear they did neither. I wish again to emphasize the fact that practically every lease that was granted in Turner Valley was granted before the transfer of

the natural resources. In any event the Government's policies were the result of the best study we could give to the situation with the advice and assistance of the best advisors we could obtain.

4. On page 8251 and 8252 the statement is made that as a result of my enthusiasm for the plan of rationalizing the oil industry " a compact was entered into between the Imperial Oil and the U.F.A. Organization" and that "this compact provided the Government, the Government political machinery which was then the U.F.A., with an income permitting it to maintain its position," etc., As this contract is the subject of lengthy discussion commencing on page 8272 of the evidence and will probably be the subject of further evidence I think it is advisable for me to place before this Commission the facts with respect to the formation of this contract.

Some years prior to 1934 the United Farmers of Alberta decided to engage in the co-operative distribution of farm supplies and entered into contracts with respect to various commodities such as binder twine, wire, fence posts, etc., and in due course ~~entered into~~ a contract with Great West Distributors Limited for the supply of oil and petroleum products. For this purpose a subsidiary organization was incorporated known as U.F.A. Central Co-operative Association Limited and the said distribution business was carried on by that organization. I wish to say emphatically I had nothing whatever to do with that decision nor with the formation of any of the contracts during

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the time I was Premier of the Province. I was not consulted nor gave any advice with respect to the incorporation of the U.F.A. Central Co-operative Association Limited, and had nothing whatever to do with the contract which they made with Great West Distributors. Some time after I resigned from the Premiership I was invited to attend a conference in Exmonton of the various local bodies associated with the U.F.A. Central Co-operative Association Limited in the distribution of these supplies. As a result of two days' discussion two facts emerged, first, that those present felt that this activity could be extended, that is by handling other commodities, and secondly that there was considerable dissatisfaction with the operation of the contract with Great West Distributors Limited. I was asked if I would undertake a survey to consider what other commodities might be handled by the organization, and later, as it became apparent that the contract with Great West Distributors Limited would be discontinued I was asked by the Executive of the organization, that is the U.F.A. Central Co-operative Association Limited, if I would undertake to negotiate a new oil connection. Without naming the various companies interviewed by me I may say that I travelled from Vancouver to Eastern Canada and to the cities of Chicago and New York meeting the more important of the independent companies in the United States who were at all interested in distribution in Canada. Now Sir, my Lord, since typing that I have discussed the matter with the officers and officials of the

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U.F.A. Central Co-operative Association Limited, and they are not at all adverse to me detailing for your information a little more definitely just what was done in that connection, because this contract will probably be the subject of considerable discussion later, and it was felt you should know what steps were taken. I may say that my first step in trying to negotiate that new contract was to go to Vancouver and to approach the officials of the Shell Union Oil Company. It was felt by myself and those who were talking with me that a new connection could probably best be made with some organization that had not yet established itself in the Province and in which there would be no comflict with their distributing agencies throughout the Province. I saw the Manager of that Company in Vancouver, and later at his request, met the Board of the Shell Union Oil Company in New York, and the Manager of the Eastern Canadian Division in Toronto. I next approached the Union Oil Company and the Manager of that Company here in the Province of Alberta will verify that. Then I approached the Texas Company and the Manager of that Company in Calgary will verify that. He presented me with a letter of introduction to the President of the Company in New York, and I met the Board of that Company in New York at the same time that I met the Board of the Shell Union.. I met the old Barnsdale Corporation, which was probably one of the oldest refining organizations in the United States, and they sent their manager - they had entered Winnipeg and were starting to develop in this Province, - and they sent their

Manager to Alberta and he spent some time here figuring on the advisability of a contract with our organization. And I probably might say we had some discussion as to the advisability of starting a small refinery at Coutts. Mention has been made of Mr. Sackett. Well, I will deal with that when I come to it in my memorandum. Those are some of the companies that were introduced, at least we met and interviewed, as well as the Imperial Oil Company, and the reason I say that is because I want it to be understood that that contract was not simply a case of myself meeting the Imperial and making the best deal I could at the time. But it was a competitive contract made after I had interviewed all of the companies that I thought might be interested in the distribution of oil in this Province. One very old and well established independent company, that is Barnsdale, which had shortly before entered Canada for the distribution of lubricating oil, sent its Manager to Alberta, to canvass the whole situation and the discussions covered the possibility of erecting a small refinery at Coutts to supply the U.F.A. Agencies. As Mr. Sackett's name has been mentioned I may add that I first heard of him at this time through an introduction from Mr. Olson, the Manager of his refinery in Edmonton. I met him in Chicago and he later came to Alberta and submitted a proposal to the organization. In the course of my negotiations I also met Officials of the Imperial Oil Company. That Company had recently purchased the equipment at some thirty stations in Alberta from Northern Oils

Limited which had previously gone into liquidation and Mr. Halvorson proposed that these stations should be made the basis of a contract between Maple Leaf Petroleum Limited and the U. F. A. Organization and after several discussions a plan was submitted by him. When I completed my work I made my report to the Executive of the organization consisting of, as I remembers, Messrs. Robert Gardiner, Norman Priestley, George Church, Jack Sutherland and Charles Fawcett, this report setting forth the various alternative proposals which were available. As a result of lengthy discussions by the Executive at meetings at which I was not present, they decided that in view of all circumstances the proposal made on behalf of Maple Leaf Petroleum Limited was the most advantageous.

I mention these facts to emphasize that this contract was negotiated after I ceased to hold the position of Premier; In my private capacity and without any reference to any of the members of the Government of that time; and was made at the request of the United Farmers of Alberta and not on my own initiative and only after a long and extensive survey in which all of the available, well established independent concerns had been interviewed. The contract was therefore a competitive one. I may add that in entering into this contract the organization followed the practice adopted by large farmer co-operatives in the United States who have not hesitated to purchase their supplies from the larger established companies if it is in their best interests

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[illegible]

to do so. The terms of the contract have been known by Mr.Frawley, Counsel for this Commission, for some time and through him by the present provincial Government, following the investigation into the oil and gasoline business in this Province conducted by Mr.Frawley for the present Provincial Government, some time ago. I have no apology to make for the contract and in fact am rather flattered by the concern manifestly shown as to its results and incidentally wish to point out that the U. F. A. Organization under this contract is the only organization distributing gasoline in a large way in this Province and paying patronage dividends to the actual consumers of the product.

5. The remaining part of the evidence can be dealt with very briefly. On page 8252 Mr. Plotkins states:

"We find that Mr.Brownlee ended up with a retainer, I understand quite respectable, as the solicitor for the Maple Leaf Oil and Petroleum, the Maple Leaf Petroleum, and he ended up as manager at a respectable salary for the Maple Leaf, I mean for the U.F.A. Co-operative organization, and he is still in that capacity today."

I simply wish to say:

(a) I received no compensation from any source whatever for negotiating this contract other than the payment of my travelling expenses by the U.F.A. Organization.

At the time I was asked to make the survey the Organization was without funds and by reason of my long association with the Organization I offered to do the work without pay, and received no pay from any source whatever other than the payment of my travelling expenses.

(b) I have never at any time received a dollar by way of retainer, gift or otherwise from the Imperial Oil Company or any officer of that Company.

(c) I have never received a retainer from Maple Leaf Petroleum Limited and am not their counsel for the Province. I understand Mr. Roy Davidson of Lethbridge acts as their chief legal advisor in this Province. It is true that since I opened my law office in Edmonton in 1935 this Company has referred to me odd matters of business in the northern half of the Province which I have handled on a straight fee basis. While I have not caused any accurate examination of my accounts since that time I know I would be safe in saying that the total amount of these fees would not aggregate an average of more than One Hundred Dollars, in any one year.

(d) I am not and never have been the General Manager of the U.F.A. Central Co-operative Association Limited nor have I occupied any other position with that Company on a salary basis. They have asked me to sit in at the Meeting of Directors on certain special occasions when matters have arisen of a legal nature. To avoid the necessity of making special charges for these attendances or other incidental advice a retainer

is allowed me of $300.00 per year and they pay me the ordinary fees for any special work which I may do, which may add to probably another $100.00. This is the only remuneration which I receive from either the U.F.A. itself or the Co-operative Organization.

I presume this contract will be the subject of further evidence before this Commission and the terms of the contract will be made available to you. While I am on the stand at this time I can probably say in reply to the evidence obtained from pages 8272 to 8283 that this contract as it will be presented to you contains within it the full terms of the business relations of the two organizations. The entire remuneration of the U.F.A. organization is set out in that contract. There are no additional secret commissions or discounts. Out of the total commissions received under this contract the organization pays a patronage dividend to its consumer members and the balance is used to pay the operating expenses of the organization, to pay for distribution facilities, wholesale and retail, set up by the organization and it is entirely incorrect to suggest that as additional compensation facilities are being paid for by Maple Leaf Petroleum Limited by way of bonus or additional secret remuneration.

Summarizing I would say; Mr. Chairman, that in respect to each and all the allegations and charges made in connection with myself, i.e. in respect to my relations with Mr. Bennett; in respect to plans designed to consolidate the position of major oil companies; in respect to the U.F.A. contract with

Great West Distributors and again with the Maple Leaf Petroleum, Limited, allegedly for the purpose of providing funds for a political organization; in respect to my receiving a reward for my services in the way of a handome retainer from Maple Leaf Petroleum Limited; and in respect to my being General Manager of the U. F. A. Central Co-operative Association at a handsome salary, the statements of Mr. Plotkins are in each and all of these matters absolutely false. They contain no vestige of truth.

I probably may just add that I checked up this morning on arrival at the City to find the date that the contract was first made with the Maple Leaf Petroleums Limited, and I find that the contract was made on the 17th day of August, 1935. That is nearly a year after I had resigned from the Premiership of the Province. That is all I have to say, Mr. Chairman, unless Mr.Frawley or someone else wishes to ask me some questions.

MR. FRAWLEY: I have no questions.

MR. SHAW: We accept without hesitation in the same spirit the statement made by Mr. Brownlee. I certainly personally commend him for having made his presentation.

THE CHAIRMAN: That is all, thank you, Mr. Brownlee.

MR. FRAWLEY: Mr. Mercer.

....

RUSSELL D. MERCER, recalled:

Q BY MR. FRAWLEY: You are still under oath? Will you now produce the documents which I requested in my letter of the 9th? To clarify the record, Mr. Chairman, you will recall that when Miss MacAskill was on the stand on the 9th instant, she gave me a list of seven other items which she thought should be subpoenaed and as we were anxious to proceed I listed those documents without a subpoena in a letter to the Company. Mr. Mercer is now producing them. I will follow this. It may not be chronological, but I will follow it in the order I have set them out in the letter. Item Number 1. You are producing the first item I asked for which is a letter from C. D. Dean to J. H. McLeod, dated the 14th of December, 1938. Now it is a full three pages and would you be good enough to tell me, unless it is requested that I read the whole letter, what it deals with, Mr. Mercer?

A It deals with the Dominion Income Tax.

Q Of what Company?

A Of the Royalite Oil Company.

Q And Mr. C. D. Dean, as it appears from this letterhead, is the comptroller of taxation for the Imperial Oil Limited?

A Yes.

Q Or was at that time in any event?

A Yes.

THE CHAIRMAN: Mr. Frawley, I suggest that you show it to Mr. Shaw, and if he thinks it is of value to us we will let him mark it as an exhibit. If he thinks it adds nothing, we won't unnecessarily add to

the exhibit numbers. You might just get the others.

MR. FRAWLEY: And do the same here?

THE CHAIRMAN: Yes. If you want to put it in, Mr. Shaw, it will go in, and then we will have it read.

MR. FRAWLEY: It was dealt with by Miss MacAskill. Item Number 2 is a letter from the Foothills' shareholder, and that was sent on as we were told by your Company to Toronto. You have not been able to find any sending on, but this is a letter from the Foothills' shareholder is it?

A That is marked as "Foothills' shareholder " sir. I presumed that was the letter.

Q Letter June 8th, 1938. I may do the same with that, Mr. Chairman?

THE CHAIRMAN: Yes.

MR. FRAWLEY: And you say that you could find no covering letter forwarding that letter, or its copy of course, to the Imperial Office in Toronto. You see the subpoena item Number 2 there?

MR. NOLAN: Perhaps that.....

A We understood that only to be the letter from the shareholder.

MR. NOLAN: We thought that letter was a description to help us find it. It was sent on to Toronto, there is no question about that, if that is the copy of the letter that is being referred to.

MR. FRAWLEY: The point that was being made by Miss MacAskill was that it was sent to Toronto with some comments, that it was time something should be done.

Without endeavouring to remember too much of what she said.

MR. NOLAN: That some action be taken in respect to the shareholder's complaint. That is quite right. That was done.

MR. FRAWLEY: Perhaps if Mr. Mercer or Mr. Nolan will say it was just simply a formal letter forwarding the document you have shown me to Toronto, suggesting that something be done?

A I believe a copy of that letter was forwarded to Toronto.

Q Was there anything worth while in the forwarding letter, that is all?

A I did not see a copy of the forwarding letter, sir.

Q I think perhaps to clear it up you had better let us have the forwarding letter. Now the third item is a copy of the monthly letter written by Mr. McLeod to G.Harrison Smith with regard to monthly production of the whole Turner Valley field. Have you been able to find that?

A This does not really relate to production. It relates to deliveries from wells in Turner Valley to the pipe line.

Q In any event, Mr. Mercer, that is what you thought was the thing asked for in item 3 of the subpoena?

A Yes, and we took the last month.

Q Item Number 4 in the letter requesting this material is a letter from Mr. McLeod to Mr.Smith, written in September, 1938, informing Mr.Smith with respect to the interests of Royalite in the various independent companies, the net proceeds returned to the Royalite

from each company up to that date, the balance still owing, etc.

A There was no letter of that nature left our office or was prepared. At least left our office in September, 1938. However, a draft had been prepared which was never sent, nor did it leave our office. That covers, I believe, the subject that was called for. That is only a draft form.

Q This is what you feel is intended to be asked for by item Number 4 in this letter?

A Yes.

Q Item 5, a letter written within the last thirty days or so, from the Head Office of the Imperial to Royalite with regard to taking over Lowery Petroleums Limited. Letter of 10th May from Mr.Smith to Mr. McLeod. Now Item Number 6. Letter of 1st February, 1939. from Mr. McLeod to Mr.Trammell, Turner Valley, with regard to distribution of expense of production maintenance crews?

A There was no letter written from Mr. McLeod to Mr. Trammell as far as our search would show. But there was a letter to Mr. Smith at the field office covering that subject.

Q That is what is intended?

A Yes.

Q Mr. Smith is an associate of Mr.Trammell's is he?

A No sir. He is more an associate of the Calgary Accounting office at Turner Valley.

Q And Mr.Trammell is what?

A The field supreintendent.

Q Succeeding Mr.Coultis in the field?

A That is right.

Q Item Number 7, Memorandum to Mr. McLeod prepared by yourself dated the 17th of October, 1938, dealing with estimated net earnings for 1939, and stating further that the actual daily average run, pipe line run, would be in excess of 15,000 barrels.

A I have not been able to find that memorandum, Sir. I instituted a search myself through our files, and I had Mr. Patton institute a search through Mr. McLeod's files. I have also personally gone through my own working papers, and I have not been able to locate that memorandum.

Q Have you something else you are producing?

A No sir.

THE CHAIRMAN: I suppose, Mr. Shaw, you would like to look through these documents before you can examine on them?

MR. SHAW: Yes.

THE CHAIRMAN: We will have a short recess.

(At this stage there was a short recess).

Q MR. SHAW: Mr. Mercer, one letter we were talking about, I would ask to have read into the record.

THE CHAIRMAN: That will be Exhibit "298".

(LETTER PRODUCED AND HERE MARKED EXHIBIT "298")

Q MR. FRAWLEY: Exhibit "298" is a copy of a letter from?

A Mr. McLeod.

Q To Mr. E. C. Smith, Royalite Oil Company, Turner Valley, dated 1st February, 1939?

THE CHAIRMAN: Who is Mr. E. C. Smith?

Q MR. FRAWLEY: Who is Mr. E. C. Smith?

A Mr. Smith is the field clerk at Turner Valley in the Accounting Department.

THE CHAIRMAN: All right.

MR. FRAWLEY: This letter is dated 606 - Second Street West, Calgary, Alberta, February 1st, 1939, 100 - 2 - d, that is the file number I take it?

A Yes.

"Mr. E. C. Smith,

"Royalite Oil Co., Limited,

"Turner Valley, Alberta.

"Dear Sir:-

" We acknowledge receipt of your "letter No. 2561-T.V. of January 27th, File 4.0, en- "closing your memorandum regarding the distribution of "expenses of the production maintenance crews.

" We have, as you know, given a "lot of consideration to the method as shown of charg- "ing out these expenses and have always disagreed with

"it. The net result leaves us no recourse but the "conviction that we have been making charges to "contract wells in actual contravention of our agree- "ments. In other words, charges have been made to "certain wells which represent the expenses of a crew "which conceivably have not done the work which the "charges represented.

" The matter of it being a fair "charge or a fair proportion of a general charge does "not help us. We are only entitled to charge the con- "tract wells with cost for such services when actually "rendered, and under the present system the charge made may "include no actual services but a proportion of daily "time taken up by a crew other than at the specific "wells receiving the charge.

" It will be necessary that "you arrange that all foremen in charge of these "maintenance crews keep an actual record of the work "done and the time expended in hours; that this be "certified and turned in each day and that a monthly "distribution be based on this statement of actual "work done through which we shall be able to substan- "tiate any charges made to wells as having been act- "ually incurred.

" It will be necessary to state "to the Calgary Accounting Office in showing the dis- "tribution, the total number of hours the crews were "operating and the total number of hours spent on each "operation or each well receiving a charge.

" Will you please arrange
"that this be put into effect immediately and that
"no further distributions using percentages based
"on the previous method be used.
" Yours very truly, "

And what are the contract wells?

A The contract wells are wells that we operate under contract, not owned by ourselves.

Q For the sake of the record give us an example of some of them, of what were contract wells as of this date, February 1st, 1939, can you?

A February 1st?

Q At this date, the kind of wells that Mr. McLeod would be speaking about when he wrote to Mr. Smith?

A We could classify the Davies Petroleum No. 2 or Royal Canadian No. 1 as contract wells as of that date.

Q Now any others, Mr. Shaw?

MR. SHAW: The one which was marked Exhibit "298" in error, I would like to defer judgment on that if I might. This particular document is of no interest or value nor is this in our opinion. This one may have a remote interest perhaps. I am not clear about it and may I say with regard to the other one, the draft letter referred to, I am instructed this is not the letter, it was a letter sent to Mr. Smith but it disclosed, not the Northwest interests in the various Turner Valley wells but the Royalite interests in the Turner Valley wells and was written approximately about September, 1938; this particular letter was never sent and that is not the one we are concerned with.

MR. FRAWLEY: You can have that one back (hands document to witness) and then Mr. Shaw suggests, even although he suggests it is not particularly important, I think we will offer this.

(LETTER PRODUCED HERE MARKED AS EXHIBIT "299").

MR. FRAWLEY: This is a letter from the office of the President, Imperial Oil, Limited, Imperial Oil Building, Toronto, Canada, dated May 10th, 1939, No. 32 and it reads:

"Mr. J. H. McLeod,

"606 Second Street West,

"Calgary, Alta.

"Dear Sir: Re: Lowery Petroleums Limited

"" We wish to acknowledge receipt of your "letters Nos. 919 and 942 in regard to the proposed "contract between Lowery Petroleums, Limited, and "Royalite Oil Company, Limited, for drilling a well "in L.S.D.6 of Section 22, 20-3-5.

" In this connection we are enclosing a copy "of a letter of today's date to Mr. Roadhouse which "we believe is self-explanatory'

Q MR. FRAWLEY: If I might intervene, can you tell us who Mr. Roadhouse is?

A Mr. Roadhouse is in Toronto.

Q I mean is he a member of your organization?

A No, sir.

Q Do you know anything about him at all, I only interrupt to know what we are reading about?

A It is only presumption on my part but I have presumed he is

a member of Doherty Roadhouse, Toronto.

Q Stock brokers?

A Yes.

"In the meantime, and until the question of the "transfer of Lowery Petroleums' interest from "L.S.D.6 to L.S.D. 2 is settled, we would request "that the agreement between these companies be held "in abeyance.

" We think we have made it "quite clear that Lowery Petroleums should have an "interest in the well to be drilled on L.S.D.2 under "terms as identical as possible to those that would "have applied in the case of a well on L.S.D.6. In "speaking to Mr. Roadhouse this morning regarding this "matter he was of the opinion that Lowery Petroleums "should accept our offer. When the offer is accepted "on behalf of the Company, the deal can be consummated "as soon as the Company is reorganized according to "the plans already drawn up. The reorganization can "proceed immediately on the return of the agreement "between the four interested parties, which we presume "has now been executed by Royalite and returned to the "C. & E. for execution by it'

Q MR. FRAWLEY: That is a Calgary and Edmonton Corporation, the C. & E.?

A Yes.

" It has been decided that the "head office of the Company should be moved to Calgary "and that the new Board should consist of the following:

" J.H.McLeod - President
" Alexander Hannah - Vice-President
" S.F.Heard -)
" T.E.Burns -) Directors
" T.H.Roadhouse -)

" Mr. Roadhouse has indicated "his willingness to accept the directorship.

" Yours
Very truly yours,

G.H.Smith
Per O.B.H. "

And you do not know who "O.B.H." is?

A No sir, I do not.

MR. FRAWLEY: Now any others, Mr. Shaw?

MR. SHAW: No, subject to what I have said and then this other statement, instead of the draft letter, perhaps you can find out if there is a similar letter with respect to the Royalite interest.

MR. FRAWLEY: Yes.

Q MR. FRAWLEY: I have returned to you the draft letter, which it would be difficult to describe because I presume it is not dated?

A No, that is not dated.

Q Well you gave me this document copy of which I have in my hand, entitled "draft" and consisting of seven pages, 6½ pages, a draft of a letter or memorandum to Mr. G. H. Smith, re interests in various Turner Valley wells, that was in answer to the request that I made that you should produce a letter from J. H. McLeod to G. H. Smith written in September, 1938, informing Mr. Smith with respect to the interest of Royalite in various independent companies, the net proceeds returned to Royalite from each company up to that date, balance still owing, etc.

A We have been unable to find any letter of that nature written in September, sir, pertaining to that subject.

Q Well does the memorandum, you might examine it, does, is this memorandum restricted entirely to the interests or a discussion of the interests of the Northwest Company in various independent companies, you might look at it and see, perhaps it is what Mr. Shaw wants after all?

A No sir, it covers both Northwest and Royalite wells.

Q Well then just depending on the description which you got from me, does that memorandum, if it was ever sent, inform Mr. Smith with respect to the interests of Royalite and various independent companies?

A Yes.

Q In all the independent companies in which Royalite has any interest?

A I would have to check that.

Q Was it complete in that respect?

A It was complete. I would not like to say if it was complete to that certain date, Mr. Frawley, but I do know that it covers Royalite's contract wells.

Q And does it give the net proceeds returned to Royalite from each company up to that date; however there is perhaps not much point in following this up, if Mr. Shaw says, after consultation with his client, that it is not the document which we want?

MR. SHAW: Does it cover Davies Petroleum for example.

Q MR. FRAWLEY: Yes, does it?

A No, Davies Petroleum is not listed in this.

Q Now have you a memorandum there at all, having in mind the

language in Item 4 of my letter, giving to Smith information from Mr. McLeod dealing say with Davies Petroleum?

A We would have to make a further search.

Q You would have to make a further search?

A Yes.

Q So that there will be no question but that we have exhausted every effort to try and get this material, will you please do that?

A Yes, I can make a further search.

Q In the meantime I think you had better keep my letter to you?

THE CHAIRMAN: All right, Mr. Shaw.

MR. SHAW: No further questions.

TO MR. NOLAN:

Q There has been marked, Mr. Mercer, a letter Exhibit "298" dated the 1st of February, 1939, being from Mr. J. H. McLeod to Mr. E. C. Smith and you say this is written from the Calgary office to the Field Accountant?

A Field Accountant or Clerk.

Q Field clerk?

A Yes.

Q And it is discussing methods of making charges arising out of the expenses of the production maintenance crews?

A Yes.

Q Now in a word what was the sytem in vogue prior to this letter of February 1st, 1939?

A We found that the field, in distributing----

Q Just a moment, what are "production maintenance expenses", what are they?

A The salaries and routine expenses, material and expendable materials, tools, etc. used by these maintenance crews to operate the wells or groups of wells in Turner Valley.

Q All right, now prior to February 1st, how was that being distributed?

A The field was making the distribution----

Q What do you mean by the "field"?

A Field office, sir.

Q And who is in charge there?

A Mr. Smith is in charge of the field office, they passed us certain distributions which we apply against costs and they make certain distributions of payrolls which we voucher and pass through our books. Those payrolls distribution were effected in connection with the swing crews on a basis partly based on the production of the wells interested and partly based on an arbitrary distribution.

Q All right. Now there is so much expense to be distributed?

A Yes.

Q That is distributed, you are talking about contract wells?

A Contract wells along with our own wells.

Q Along with our own wells and that expense is distributed partly on the basis, was distributed before the 1st of February, partly on the basis of what these wells produced?

A Yes.

Q On the basis of their production?

A Yes.

Q And partly upon the basis of what?

A An arbitrary distribution of the----

Q Of the accounting expense?

A Yes, of the accounting expense.

[illegible]

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Q Now whose idea was that?
A That was formulated in the field.
Q Then we come to February, 1938, 1939 rather and I find that the Calgary office in Exhibit "298" is questioning that procedure?
A Yes, we questioned the distribution of those charges as part of our duty.
Q You mean when you say "we", who are you speaking of?
A The Accounting Department.
Q In Calgary?
A In Calgary.
Q Is questioning the Accounting Department in the Valley as to the method of distribution?
A Of distribution of those costs.
Q You had an idea here of your own?
A Yes.
Q And what was your idea in Calgary, how should it be done?
A We considered that cost, we considered in this connection that those costs should be distributed on an actual basis.
Q Actual?
A Yes, that the time of the members of the crew should be noted at each location and the total number of hours worked during the period would then be allocated on the actual hours of the crew at this location and be reported to us in a percentage basis.
Q And is it fair to say that by adopting that method you would get away from the arbitrary allocation of that expense?
A Yes.
Q Under the old system?
A Yes.

Q Well whose views prevailed, the Calgary accountants or the Field accountants.

A Our views prevailed.

Q And that is the way it is being done?

A That is the way it is being done at present.

Q Yes, but the other system was in the opinion of the field a fair system?

A They considered it very fair and in fact that letter had to be written in rather strong language for us to bring our point over, that we wished this basis to be put into force.

Q Yes, I think I follow that. Now Mr. Mercer, something was said here the other day about statements which had been prepared and withheld from this Commission; now you know about statements that had been prepared during the time that this Commission has been sitting?

A Yes.

Q Now to go back to the beginning, do you remember statements which were prepared when Mr. Morrison was discussing matters of accountancy with the Royalite Oil Company?

A Yes.

Q On what basis were those statements prepared?

A We prepared the statements on what we called the "revenue basis".

Q Yes, did you talk them over with Mr. Morrison?

A Yes,full discussions were made.

Q With Mr. Morrison?

A With Mr. Morrison.

Q And Mr. Morrison was the Commission accountant?

A Yes.

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Q Did he accept those statements?

MR. FRAWLEY: He is not the Commission Accountant.

MR. NOLAN: I beg your pardon, he was the accountant assisting Counsel to the Commission.

MR. FRAWLEY: With regard to pipeline matters.

MR. NOLAN: But he came to us with the authority of the Commission.

MR. FRAWLEY: Of Commission Counsel.

Q MR. NOLAN: And were they acceptable to Mr. Morrison on that basis of revenue?

A No sir.

Q Then what happened, tell us in your own language what took place?

A We had prepared these statements and after discussion with Mr. Morrison and finding that they were not acceptable to him as the basis that we had used.

Q Yes?

A We then approached our auditors on our own behalf and requested their opinion as to our statements.

Q Well now when you say you approached auditors, had this question been discussed with any auditors by the Company prior to this interview with Mr. Morrison?

A Yes, our own auditors.

Q Our own auditors?

A Yes, the company's auditors.

Q And who were they?

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A Price, Waterhouse and Company.

Q And what attitude did they take about it?

A They didn't accept the basis we had used either.

Q And that you told me was the revenue basis?

A The revenue basis.

Q Well what basis did they want?

A They wanted to use the labour ratio basis.

Q You mean the Price, Waterhouse basis?

A Yes, that was the basis of that.

Q And is it fair to say that they declined to put forward statements prepared on a revenue basis?

A Yes.

Q And I understand and we know here that Mr. Morrison proceeded also on a labour ratio basis?

A That is my understanding of it.

Q In precisely the same as the Price, Waterhouse, but the point I am trying to make with you is this, that the statements which were prepared and not submitted were on the revenue basis?

A Yes.

Q That basis was not acceptable either to your own auditors or to Mr. Morrison?

A That is quite correct.

Q And that is the reason they did not find themselves here before this Commission?

A Yes.

Q MR. FRAWLEY:

Q And those statements which you produced which were subpoened from you at Miss MacAskill's request and which are here, put in the other day, you know the statements that Miss

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MacAskill has put in, statements showing cost of production, showing Imperial Oil's interests perhaps I should say in certain production in Turner Valley?

A Yes.

Q The cost figures, you know the statements to which I refer?

A Yes.

Q You produced them here yourself in answer to the subpoena served some days ago?

A I think I understand.

Q Those statements were prepared on a revenue basis?

A The foundation of those statements were prepared on a revenue basis.

Q It seems you informed your head office in Toronto and they perhaps informed the head office, of that I presume you have no personal knowledge?

A No.

Q Of costs built up on a revenue basis?

A That is correct.

Q And as I understand you anyway and I have always understood Mr. Burns to say that those costs contained essentially a number of assumptions as to the distribution of indirect costs?

A That is correct.

Q An assumption of revenue, of being the revenue basis?

A Yes.

Q And that, Mr. Morrison thought and your own people thought, was quite inadequate for the purposes of this Commission?

A That was my understanding.

Q However good they might be for your own purposes and for

your President's purposes, they were not good enough for the purposes of the Commission examining into the cost of transporting a barrel of crude oil through your pipeline, that is the fact, is it not as you understand it?

A That is my understanding.

Q And what the objection was by Mr. Morrison and Price, Waterhouse----

A That is so.

Q It is not necessary now to go into, but they built it up on a quite different basis?

A Yes.

Q Do I understand you people continued to make these statements for your own internal purposes notwithstanding Mr. Morrison's views as to what might be enough for this Commission?

A I have prepared the statement for the year 1938 at the request---

Q Exhibit "255"?

A Yes.

Q Which is the Jersey statement for the year 1938?

A Yes.

Q But I was referring to these other documents which were here the other day that Miss MacAskill produced?

A Yes.

(Go to number 8829)

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

R. D. Mercer

Q MR. SHAW: With regard to Exhibit "298" which you have before you, and your evidence indicating some difference of opinion as to the bases of charges against the contract well. Can you tell me whether that difficulty had arisen before, or was that a continuing difficulty you had with the people in Turner Valley?

A This letter came about by our...........

Q MR. FRAWLEY: When you say "this letter", would you refer to the Exhibit number?

A Exhibit number "298". Last year or about that period of time, our operating system of operating wells has changed to the extent that we now operate a series of wells with a single crew instead of using individual crews at individual wells. The expenses of those crews are being located as I explained.

Q MR. SHAW: You say in an arbitrary way?

A Partially arbitrary, and partially based on the production of the wells being operated. The Accounting Department then objected.

Q Can you tell me whether the companies concerned with whom you had contracts objected or made complaints with respect to the allocation of the costs or charges generally?

A I have no knowledge.

Q You would not have any knowledge of that?

A No.

Q Can you tell me whether, having prevailed with your views that the system of charges up to the 1st of February, 1938 was in error, can you tell me whether there was any rectification to those companies in respect of that policy which you had followed and which you found

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to be unfair to them?

A On taking this matter up with our field office and going over the whole subject, we found that any differences were very, very slight, if any.

Q Your field office finally convinced you that it did not amount to very much?

A It did not amount to very much, although we put in our system as being the more correct and having better substantiation for the charge.

Q And that has been in effect since the 1st of February last?

A Yes, sir.

Q Has the subject of these charges against these contract wells been considered or been before this Commission previous to the 1st of February, 1939?

A I would not know.

A MR. FRAWLEY: I have these Exhibits I wanted to speak to you about. Take for instance Exhibit "289" and Exhibit "290", which are cost statements for the years 1937 and 1938 respectively. Taking perhaps "290" which is the statement for 1939, you have a cost per barrel there of crude oil of $0.7845, or about 78½¢ a barrel?

A Yes, sir:

Q Now, on what basis is that figure of 78½¢ arrived at?

A On the revenue basis.

Q And this was prepared roughly at what time? Dated..... no.

A For the year 1938. It would be during this year.

Q Yes.

A During this past winter or early Spring. It would be prepared then, yes.

Q Is that prepared once a year or is it prepared monthly, statements of that kind?

R. D. Mercer

A This statement would be prepared twice a year.

Q And the last one you made then, was when?

A For the year 1938. The last one is Exhibit "290" that you have in your hand.

Q Yes. Are you still keeping cost records for the purpose of making out statements of this kind, Exhibit "290"? Are you still keeping cost records?

A I will make a record so that I may submit this class of information called for.

Q You probably will be sending out to Toronto on the same sort of form, built up the same way as built up in "290", in the future?

A Yes, sir. I might qualify that if I may. We have used this basis of cost in costing inventories of oil that may be on hand at the end of any accounting period. We anticipate still having inventories at the end of future accounting periods, and until I am instructed to put into force a new system, I anticipate making up these memoranda of costs for the purpose of inventory and I also use them in any statistical data that I may be called to give the executive.

Q And you will continue to use the revenue basis?

A As far as I am concerned to date.

Q Just while we are referring to that. Is there any significance attached to the letter, Exhibit "298", from Mr. McLeod to Mr. Smith, because that is an item of cost going into the cost per barrel of crude oil, is it not?

[illegible]

A Yes, sir.

Q Now, what basis do you use for distributing those expenses, utilities crews in making up these statements such as Exhibit "290"?

A The cost of the utility crew would find its way into our direct operating expense.

Q So now the question of the distribution on a revenue basis or some other basis does not apply in connection with the cost of production in Exhibit "298"?

A No.

Q Those are direct costs?

A Yes, those are direct costs.

Q How do you know how much time your production and maintenance crews spent on Royalite wells as distinguished from some of the contract wells?

A The foreman is instructed in that respect to verify the time spent by the members of the crew at each location.

Q Yes. Oh, well now, that is for the year 1938, is it not. He did it on some other basis?

A He did it on a comparison of the production of the one well to another for a portion of the expense and the balance of the expense was split on an arbitrary basis, based on the men's knowledge.

Q Leaving the contract wells, as you call them, aside, and thinking only of our desire to find out what it costs the Royalite to produce a barrel of crude oil. Looking at Exhibit "290", which shows the cost for 1938, and looking at the figure of 78½¢ which is called "Royalite cost of production for 1938 for crude oil", would you say that there is any infirmity in that figure of 78½¢ in view of what you have just told me of the

matter of distributing the expense of production and maintenance crews?

A Only the general remarks that have been made against the Jersey statement.

Q Yes. As I understand though you now are going to endeavor to get the production and maintenance crews to be exact, and you know how much they spend on Royalite wells and on contract wells?

A Yes.

Q I take it from now on you will have something that at least satisfies you that you know where that kind of expense has been incurred?

A Yes.

Q In 1938 you say it was done on an arbitrary basis, the percentage of production from Davies Petroleum as compared with Royalite No. so and so. Do you see what I mean?

A Yes.

Q You do not think that is completely accurate, do you?

A Unless insofar as a method of distribution.

Q Whatever there was wrong with it, you thought it was worth while to change?

A Yes.

Q You think now you have a better system than 1938?

A Yes, in allocating these direct costs.

Q The particular kind of cost that is reflected in the 78 and a fraction cents that is put down in Exhibit "290". It is put down as the cost of producing a barrel of crude oil in Turner Valley by the Royalite in 1938?

A Yes. It is a portion of those costs.

R. D. Mercer

Q It is in there?

A Yes.

Q In this what you call arbitrary, and perhaps you might go so far as to say unsound distribution of that particular kind of cost?

A It is a proportion of that is related in the 78½¢$\frac{3}{4}$

Q You have not anything more recent than 1938, which is Exhibit "290"?

A No.

Q Let me understand again, following up Mr. Nolan, why this document, this thing, or that kind of information, was not submitted to the Commission?

A We did not consider that it was of interest to the Commission. The background of the statement was made on a revenue basis, of cost, and as Mr. Morrison, the auditor did not agree to that basis, we did not consider it was of interest to the Commission.

Q That is with regard to the pipe-line.......I just want to understand and to be perfectly clear about Mr. Morrison. As you know, his connection with the Commission ceased when we discontinued attending to pipe-line matters?

A I understand.

Q And Mr. Burns has already made a statement with regard to the cost of production?

A Yes.

Q Of Royalite oil, and some of the companies you are managing?

A Yes.

Q Such as West Turner?

A Yes.

THE CHAIRMAN: What was that Exhibit number, Mr. Frawley?

R. D. Mercer

MR. FRAWLEY: I was trying to find it. In connection with Royalite?

THE CHAIRMAN: The Exhibit number in which you found the 78½¢ figure.

MR. FRAWLEY: That was Exhibit "290" that I have just been examining him on.

THE CHAIRMAN: Then Mr.Burns' statement, what is the number of that?

MR. FRAWLEY: I have been looking for thellast two minutes.

THE CHAIRMAN: Do you remember, Mr. Nolan?

MR. NOLAN: No, I have not my reference here.

MR. FRAWLEY: I have this document put in by Mr. Burns, West Turner Wells. Exhibits"237", "238", and "239". Clearly, there are some other Exhibits.

THE CHAIRMAN: Yes, there is Mr. Burns' own statement.

MR. FRAWLEY: If I had my record of Exhibits I might refer to the number. I want to do that before this witness stands down, compare these two things.

Q As I say, Mr. Morrison left us when we finished dealing with pipe-line matters. Mr. Burns then made a submission, as best he could, I am sure, with regard to the cost of production of Royalite oil. I presume you assisted him in the preparation of those statemants, did you?

A No doubt I did.

Q Do you know if he submitted to us a cost of production based in any fashion on the revenue basis of distributing indirect costs?

R. D. Mercer

A I would like to inform myself on that method. He made that statement up.

Q MR. FRAWLEY: Yes. Then let me ask you, and I am saying it in a friendly way, why did not Mr. Burns show us this statement Exhibit "290"?

A This statement only shows the final Imperial's proportion of the cost as pertain to its holdings in the company.

Q As a matter of fact, I do not recall that, but it may be just this figure Mr. Burns did give us for Royalite crude oil 78½¢ per barrel, and $1.34 for separator naphtha, and $1.41 for absorption plant naphtha. But that is the figure I would like to bring to your attention?

A Yes.

THE CHAIRMAN: Well, we will find it.

Q MR. FRAWLEY: You say again that the reason that document was not produced.....and I think I understand it now...... the reason that document was not produced in connection with the pipe-line matter. But I am more concerned now as to any value it may be to us with regard to the cost of production. What have you to say about it, whether the Commission would be entitled to take from you now, on behalf of Royalite, a figure of 78½¢, roughly, being its cost of producing crude oil in 1938?

A No, sir, I do not believe that could be taken.

Q Why, Mr. Mercer?

A This statement, which comes from the Jersey statement?

Q Yes?

A Is prepared by me in the course of closing the books of the company for an accounting period.

[illegible]

[illegible]

[illegible]

[illegible]

R. D. Mercer

Q Let me go right to that, so the Commission will have it on record. The witness is referring to Exhibit "255", which is the Jersey statement for 1938?

A Yes, sir.

Q You are referring to the figure in Exhibit "290" of $0.7845 per barrel?

A Yes, sir.

Q And will you refer to any similar figure in Exhibit "255", the Jersey statement for 1938?

A This will show just the point I wanted to bring up. These figures ....

Q In what? Whenever you say "these", refer to the Exhibit?

A The figure $0.7845 per barrel on Exhibit "290" was taken from a draft statement prepared by me during the course of closing the books of the Royalite Oil Company so that I might price the inventories of oil held at the end of the year. Of necessity, they are prepared in a hurry, only a matter of two or three hours is taken to go over the whole books of the company and take the figures down. Then in preparing this statement.......

Q This statement, Exhibit "255"?

A Yes, the statement, Exhibit "255" which was submitted to the Commission I was able to go over and spend more time and I find the figures shown on Exhibit "290" of $0.7845 is now reflected on this statement, which is Exhibit "255", as $0.7876.

Q $0.7876 is the cost of producing crude oil by Royalite in 1938?

A Yes.

Q Using the revenue basis?

A Yes.

R. D. Mercer

Q When did you prepare these two statements, in point of time, Exhibit "255" and Exhibit "290"?

A The information used on the cost in making up Exhibit "290" was prepared roughly during the first two weeks in February.

Q 1939?

A 1939.

Q And Exhibit "255"

A I do not know the date on which this was submitted by Mr. Burns, Mr. Frawley.

Q On the 16th of May, the Chairman told us?

A Then this Exhibit would be finally prepared the second week in May, 1939.

MR. FRAWLEY: Is that right, Mr. Chairman, Exhibit "255"?

THE CHAIRMAN; Yes.

Q . MR. FRAWLEY: You say Exhibit "255" was prepared more carefully by you?

A Yes, sir.

Q But again, as I understand your company, subject to the infirmity for Commission purposes of being prepared on the revenue basis?

A Yes.

Q Well, let us discuss that for a moment.........

THE CHAIRMAN: This witness tell us that notwithstanding what has been said to him by auditors in respect to pipe-line matters, with which we are not now concerned, that they continued to use the revenue basis to arrive at their.......for inter-office purposes ......the cost of producing the crude oil.

R. D. Mercer

MR. FRAWLEY: Yes.

THE CHAIRMAN: Now, it may be that he is right, and that is the right way to do it, as the company is not doing anything foolish, I suppose. I would like to know more about it. Perhaps his view will prevail with us rather than that of the auditors. Let us hear why. Pursue it.

Q MR. FRAWLEY: Yes. We will just forget all about the pipe-line. This revenue basis statement might have been no good for pipe-line, but that is history now. We are concerned with the cost of producing crude oil. Is there anything wrong with the distribution of indirects on a revenue basis when one wants to find out the cost of producing crude oil by your company?

A It can be argued that a certain Department handling higher-priced products will have a greater revenue and of necessity then stand a greater proportion of the indirect cost than really should be applied, Mr. Frawley. That is a criticism against the principle of using the revenue basis as an allocation of indirect expense. It might over-load a certain Department with an onerous overhead. We use this only to evaluate what we have considered in the past a very small inventory of oil. It has never been a large amount of money on each balance sheet, and it has always proved at least equitable for the purposes for which it was used.

Q Of........

A Of evaluating our inventories of oil.

Q Let us just see what these alleged infirmities are of the indirect bases of distributing. I seem to remember it means unless the Department with respect to which you

desire to allocate costs is a non-revenue producing Department it is not charged with any portion of administration, for instance.

A That is true.

Q So that your Department, the Drilling of Wells Department, is not a revenue producing department?

A No, sir.

Q So that now having only in mind crude oil, it means that the salary of the General Manager, Mr. McLeod, is not charged with any portion of.........yes, it seems very familiar.......but it is the same thing, is it not? You know what I am speaking about. No part of Mr. McLeod's salary is charged to the Drilling of Wells Department?

A That is true.

Q If, while you are drilling some wells over in this subdivision, you are producing some crude oil in this legal subdivision, nevertheless, no part of the salary during that period goes against the Drilling of Wells Department?

A Yes.

Q And I take it perforce more must go against the Producing of Oil Department than otherwise would go?

A Yes.

Q That is the situation. We need not labor that. That is a suggested infirmity in that system of allocating?

A Yes.

Q Why do you continue to say it is good enough, why do you think you surely have the right cost for any purpose, valuing inventories or anything else?

A It does distribute our total profit and loss for the year,

R. D. Mercer

any year or a period under review. We are able to take our revenue and our direct and indirect cost applicable to the development and production of oil and apply them on that basis.

Q But costs. I am thinking of the 78 and a fraction cents a barrel that appears on Exhibit "255" and "290". One would think when it was put forward on two statements by your company that this Commission might be well excused and take it that is the Royalite's submission for the cost of producing crude oil in 1938. I do not want to be unfair to the company. You have now said to me you do not think that is the right cost?

A No, it is a matter of production taken from the wells in the period under review. We would have new producing wells that would produce at approximately, at flush production this year.....

Q Yes.

A At an approximate average cost of production. That must also be taken into consideration in arriving at the true cost.

Q Yes, I see that. That is a little different, is it not? That is another infirmity, another difficulty that presents itself in trying to get the cost of production of the company at all if it has different kinds of products and flush production and older production

A Yes. Another point, to take our basis we would have to give the true cost of producing we would have to wait until we had obtained the last barrel of oil out of the ground.

Q Yes.

R. D. Mercer

A To get the true basis on this principle.

Q Yes, I see that, too. I am just concerned with why you are advising Mr. Smith or anybody else through him that your cost of production in 1938 was 78 and a fraction cents?

A We have always taken the information which we have supplied the executive as more a figure, not a natural figure, but more of an opinion by comparison?

Q What do you mean by that?

A That we may report for the year 1937 that certain costs are so much.

Q Take this figure, looking at Exhibit "289", what was the figure of Royalite's cost of production in 1937, which is what Exhibit "289" states in part?

A The Royalite cost of production of crude oil on Exhibit "289" was $0.7475 per barrel.

Q With certain costs excluded?

A Excluding the gathering costs, yes.

MR. COMMISSIONER LIPSETT: Is that Exhibit "289" for 1937 or for the first half of 1938?

A It is to June, 1938. That is quite correct.

Q For the first six months?

A Yes.

Q That is what I had. 1937 is not here.

MR. FRAWLEY: I am sorry, Exhibit "289" is for the first half of 1938, and Exhibit "290" is for the complete year, 1938?

A Yes.

Q Then this is of no particular value because it clearly is broken off, the accounts are broken up in Exhibit "289" but I presume it to be all there in Exhibit "290".

MR. COMMISSIONER LIPSETT: What is "291", that is 1937, is it not?

THE CHAIRMAN: Mr. Frawley, I may mention it now. As I recall the position of both auditors, it was that a labor ratio basis should be used.

MR. FRAWLEY: Yes.

THE CHAIRMAN: In determining these costs with which they were then concerned, in connection with the pipe-line, and so far, no one present has any idea of arriving at cost on a revenue basis. Differences of opinion are all as to whether capital labor should be taken into account or not. Now we have a witness producing a document which has been put forward to us as an inter-company account of what it costs, amongst other things, what it costs them to produce a barrel of crude oil. The witness suggests that the probative force of that statement in that regard should be not given too great weight for certain reasons he advances. But it would appear consistently and persistently the executive officers of this company have been content to accept it, and I am only saying this now so that over the noon hour you can think about it, I would like you to go on and I would like to see that pursued. If they have no interest in the cost of a barrel of crude oil, why have they consistently and persistently reported on it. And if they have an interest, why wouldn't they take the most accurate way of reporting. That may be all simply cleared up, but it would help us if it were. That is all.

MR. FRAWLEY: Very well, sir.

(At this stage the Hearing was adjourned until 2:00 p. m.)

2:00 P. M. Session

THE CHAIRMAN: Mr. Frawley, before you commence I think that I should say that it has occurred to me that by my silence in not mentioning Mr. Le Sueur when making mention of Premier Aberhart in connection with the letter, Exhibit "284", I might by my silence seem to cast a discredit upon him. It is, we think, not unusual that those who feel that their interests may be affected, should endeavor to ascertain what legislation may be passed that may affect their interests. We see nothing dishonourable in the doing of that and, as Mr. Plotkins has pointed out, apparently it is not uncommon to even approach members of the Legislature to point out what would be unfortunate legislation if passed, in the opinion of the person doing the approaching. I only mention this so that we should not by our silence with respect to Mr. Le Sueur seem to cast discredit upon him while exonerating the Premier of the Province.

With regard to Mr. Hill it is enough to say that we have placed reliance upon his evidence, which we would not have done if we had thought that he was a dishonest man.

MR. FRAWLEY: Thank you.

THE CHAIRMAN: I think that closes the whole of these matters which have recently arisen. You may now proceed with the witness.

RUSSELL DANFORTH MERCER, having been recalled, continued examination by Mr. Frawley,

Q Mr. Mercer, I was asking you this morning about the Exhibits "289" and "290" and a further one I want to show you, of Exhibit "286", all of which contain statements entitled

R. D. Mercer

"Turner Valley" and would appear to be, among other things, would appear, among other things, to indicate the cost of producing crude oil by the Royalite Oil Companies in respect of those periods with which they deal and I want to show you now Exhibit "246", which was Mr. Burns' submission with respect to the experiences of Sterling Pacific Wells No. 3, 4, 5 & 6, those are, can be generally referred to as Royalite wells I take it?

A Yes.

Q And Mr. Burns told us that he merely selected those for reasons which I need not recall now, because they seem to indicate a typical operation and he told us that there was the cost there, his statement Exhibit No. 246 shows that there was a cost of production there for a ten year period of $1.01 per barrel , now can you, by looking at this very brief statement, indicate whether or not it is prepared on the same basis as was used when the figure of 78½ ¢ was set down in Exhibit "290" or the figure of 74 ¢ set down for the year 1937 as shown on Exhibit "286", can you tell me?

A No, the figures of cost are not arrived at on the same basis.

Q We have been talking this morning about the revenue basis for distributing indirect costs and we heard what you had to say about that, what basis did Mr. Burns use in arriving, what basis did Mr. Burns use for distributing indirect costs as shown on Exhibit "246"?

A He only made an application of what he anticipated would be the cost over the period in his consideration, what he

considered would be the proper cost over the ten year period.

THE CHAIRMAN: Predicated on the revenue basis or an estimation or what?

A No, it was a straight estimation.

Q When you are estimating something, you must have some process of reasoning?

A On what we know from the past.

Q MR. FRAWLEY: No, but there are certain costs which mu be distributed, or administration for instance must be distributed?

A Yes.

Q Now how did Mr. Burns distribute the administration costs in dealing with these four Sterling Pacific Wells in Exhibit "246"?

A He took the figure of $15,000.00 per year as an estimation that that would be the amount that should equitably be allocated against the cost of producing crude oil in the Section 33 area.

Q For administration I mean?

A For administration, general, legal, technical, and other purposes.

Q I see.

THE CHAIRMAN: I am afraid I do not follow that, would you just state that again.

Q MR. FRAWLEY: Just answer that again.

A The figure of, the amount of $15,000.00 per year for a term of ten years was taken to cover the costs of administration, general, legal, technical, and other charges which would be applicable to the cost of produc-

ing crude oil in Section 33.

Q THE CHAIRMAN: Now is it your suggestion that figure is arrived at arbitrarily or how?

A That was an arbitrary figure based on experience, on Mr. Burns' conception of what should be used.

Q Based on an experience which was calculated how, the revenue basis?

A I do not believe the revenue basis was taken to lead him to authorize a charge of $15,000.00 per year.

Q You see what I am getting at, your past experience would be reflected in the figures?

A Yes.

Q Your year figures?

A Yes.

Q And how were those figures arrived at, by applying the revenue basis?

A No.

Q Or the labor-ratio basis, or what?

A No, on the total cost of our administrative expenses and legal, technical, and other expenses, we only took our past experience in the amount of those charges and at that it was considered that $15,000.00 a year would be sufficient to allocate against the cost of producing crude oil in that area.

Q Now take administration, how would you arrive at what proportion to charge to that particular phase of your operations?

A It was only an estimation.

Q But you said an estimation predicated upon past experience

and what I am trying to arrive at, how was the past experience made up?

A Only through the past experience and the amount of administrative and general expenses.

Q MR. FRAWLEY: In all?

A In all.

THE CHAIRMAN: But how divided?

Q MR. FRAWLEY: How about the distribution?

A We had no past experience insofar as distribution was concerned.

Q Oh well, didn't you, you had the revenue basis?

A Yes, we had the revenue basis only to distribute the costs against the total production. Here we are distributing costs against a product in a special area.

Q You had X thousand dollars for the total expenses, administration and so on?

A Yes.

Q And you took $15,000.00 of that X thousand dollars and set it down as against the Sterling Pacific Wells?

A Yes.

Q Now in what proportion, acreage, estimated production from all the wells as against the production from the Sterling Pacific or what, you see what I mean don't you?

A Yes, I would say ---

Q THE CHAIRMAN: Did you do the work under Mr. Burns?

A I did the work under Mr. Burns' instructions.

Q Quite so.

A Yes and it was a matter of allocating a round sum.

R. D. Mercer

Q MR. FRAWLEY: Yes?

A In the past in making the cost of producing crude oil as a whole and using the labor-ratio basis or the revenue basis rather, we are dealing with a product produced throughout the field; here we were dealing with the cost of a product from a specific area and it was considered that $15,000.00 per year would amply cover, would be the fair charge to allocate in that instance.

Q Well you perhaps discussed it with Mr. Burns, can you recall now your dicussion?

A He just considered other figures and finally arrived at the conclusion that $15,000.00 would be fair for these Sterling Pacific Wells.

Q THE CHAIRMAN; No one is suggesting it is not fair for the moment, we are just trying to find out how you got the figure, perhaps it is more than fair, but still how did you get it?

A No doubt in any discussion that went on the question of ultimate revenue from the area would be taken into consideration.

Q Mr. Frawley: Yes, you see you might have thought that these Sterling Pacific Wells were going to be, well not the worst wells in the company's operations in the next ten years, perhaps better than average, I am only making the suggestion to you as to how you arrived at the $15,000 figure, was it on the basis of estimating revenue from these wells as compared with estimated revenue from certain other Royalite Wells or how?

A The revenue, if taken into consideration, we did strike a figure of $15,000.00, it is quite an arbitrary figure

and the revenue would be taken into consideration as to what the total amount we would consider would be suitable for the area.

Q Do you think that predominated, your idea what the revenue would be?

A No, Sir, I do not think it actually predominated, it would come up for discussion though and be mentioned.

Q MAJOR LIPSETT: Can you give us the total figure under all these headings, Mr. Mercer, and then split up that whole figure among everything amongst which it should be split up, including this $15,000.00?

A I do not quite understand your question.

Q This $15,000.00 is part of a large figure?

A The item is classified under indirect expenses on Page 2, of $150,000.00.

Q Yes, and that $150,000.00 is so much out of a larger figure for indirect expenses over the ten-year period?

A Well we considered the $150,000.00 is for the ten year period, making $15,000.00 a year average.

Q As a part of this large sum which covered all the administration and general expenses and other indirect charges, now can you give us the total figure under those indirect expenses, either average or for the total period and show how that is split up among all the different departments to which part of it is charged?

A Well we never make an actual distribution of any administrative expenses or general expenses and anything we have done to split those for statistical purposes, we have done either ----

Q Mr. Mercer, as I see it, these indirect expenses cover yourown wells, cover pipe line, cover these particular wells and cover a number of other phases?

A Yes.

Q Well now, can we get the proportion or the sum of the total figure which is allocated to the other departments so as to show the whole figure, not simply this allocation to these wells?

MR. NOLAN: Of course, Mr. Commissioner, we never did that.

MAJOR LIPSETT: Then this figure, Mr. Nolan, as I see it, does not give us any assistance. We know now the pipe line, the allocation to that, and if this which is allocated, and correctly allocated we will assume --

MR. NOLAN: It was allocated for us on the pipe line, we did not do it.

MAJOR LIPSETT: Yes, but we have it now and I am asking what was the total amount and how much was allocated I want that done to see how the whole figure was obtained?

MR. NOLAN: The $150,000.00?

MAJOR LIPSETT: No, the total of these indirect expenses over the whole period.

MR. NOLAN: But they are the $150,00.00.

MAJOR LIPSETT: That is the allocation of a much larger sum.

MR. NOLAN: Yes.

MAJOR LIPSETT: $150,000.00 out of the larger sum is allocated to these particular wells?

MR. NOLAN: Yes.

MAJOR LIPSETT: What I would like to get would

be the total sum or the average sum and how it is all allocated on any basis.

MR. NOLAN: But it is not.

MAJOR LIPSETT: Well then how much is left for the other services?

WITNESS: You see it is rather difficult, Mr. Commissioner, that of our total administration costs, total administrative and general costs, in the case of the pipe line a certain proportion was allocated on the labor-ratio basis.

Q MAJOR LIPSETT: In the Jersey statements?

A No, Sir, the Commission statements.

Q First of all the Jersey statements and then in the Price, Waterhouse statements and then in Morrison's statements?

A We never made any distribution, that is our Accounting Department never made any distribution of expenses on a labor-ratio basis; part of our administrative and general expenses have been allocated to pipe line on that basis.

Q The labor-ratio?

A Yes, and that leaves the balance.

Q MAJOR LIPSETT: That was in the Jersey statement?

THE CHAIRMAN: No.

A No, Sir, that was in Mr. Morrison's statement and the Price, Waterhouse statements

Q MAJOR LIPSETT: And in the Jersey statements before on the revenue basis?

A On the Jersey statements we did distribute administrative and general costs on a revenue basis against our products

and our pipe line.

Q MR. FRAWLEY: But that was after, you did that work in connection with the pipe line after the money was spent and it was just a matter of distributing those costs fairly?

A Yes.

Q Now you are going to try and tell this Commission, - Mr. Burns did in Exhibit "246", - what it is going to cost over a ten year period from now on, to produce oil from those four Sterling Pacific Wells?

A Yes, it is a considered opinion.

Q And when you come to administration and general expenses you have to allocate something?

A Yes.

Q There is no total of which this is a distributed part?

A No, it is only an anticipated amount.

Q That you will have to spend out of your total administration, I take it, to get the oil out of the Sterling Pacific Wells?

A Yes.

Q And I do not suppose you can tell us, in 1938 they had one complete year of controlling the Sterling Pacific Wells?

A Yes.

Q Well supposing you had, you could tell us in 1938, and I submit to the Commissioner that is about all he can do, he can take the actual figures in 1938, now you have spent all your administration, all your general and all of your legal in 1938 and if it were put to you, I suppose you could make a distribution of 1938's legal and general administrative which should be allocated to the Sterling-Pacific Wells, could you?

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

A On the basis of revenue?

Q On some basis?

A That could be done I believe.

Q And that is the only basis which you have ever used yourself in your company to distribute these indirect expenses of administration and general?

A Yes, but the distribution has only been made for statistical purposes.

Q I understand but for whatever purpose it has been made that is the only system you use?

THE CHAIRMAN: He would not really know then, I suppose, as to whether or not his calculation for 1938 was accurate because he would not know how long the well would last, nor how much it would cost in its later years when the days of flush production were gone?

A That is right.

Q And that is what Mr. Burns has tried to do in Exhibit "246" by looking ten years ahead and figuring a certain cost for pumping, I mean a certain cost for natural life and a further cost for pumping life?

THE CHAIRMAN: Yes.

Q MR. FRAWLEY: That is what I had in mind this morning when I wanted you to look at Mr. Burns' submission, which you have now looked at. Now I wonder if you have anything more now in answer to this general question, looking at the figure which you reported to the company, along with a lot of other information, on Exhibit "290", the figure of 78½¢. a barrel about?

A Yes.

[illegible]

Q Now have you anything more to say as to why the Commissioners should not take that figure as representing at least the cost for 1938 for all of the Royalite production?

A That figure is taken from the original statement, the same as Exhibit "255", "255" was a revised statement.

Q A Jersey statement?

A Of the Working Sheet that I had from which I took this information.

Q Yes?

A The Jersey statement; takes up all the features of profit and loss of the company during the year's operation under revenue.

Q Yes?

A It only takes into consideration such entries as are actually booked for depletion; there being the amortization of lease and well costs, well development costs, under the basis of the allowance to the company by the Income Tax Department, that depletion amount booked is hardly a true reflection against any individual year's operation for the true costs; depreciation of physical plant as distinct from depletion of development costs and lease costs again is taken in the Jersey statements on the basis which we claim under the Dominion Income Tax Act; again that in some cases may not reflect the actual life time of the equipment used; that again would tend to destroy the value of that as a true cost.

Q Is there anything else, because I would like to get on the record everything you have to say by way of warning to the Commission with respect to taking, in your opinion, to taking that figure in Exhibit "290" as the true cost?

A There is also the question as to the inclusion of any figure of interest on investment as cost. Interest on investment is an item that is never booked, entered in the company's books, but in some instances is accepted as part of the cost. Nothing of that nature has been included in that figure.

Q Yes?

A As to the cost taken up, we have taken the actual out-of-pocket expenses of the Company in their general operations. We have distributed all those costs either directly to the products and services designated on the original statements and applied the indirect costs on the amount of revenue derived from each of the departments. It might also be mentioned that in doing this you are dealing with different products and services that have different, that return to the Company different amounts of revenue per unit. This might also distort the proportion of indirect expense to the different products. In that case one product might be half again as valuable to the Company as another product, and in that way it would return to it more revenue and naturally more indirect costs would be applied against that revenue. That might be a detriment to arriving at the true cost.

Q These are some of the things that you point to as infirmities?

A Yes, I have tried to give the matter some consideration

and those are the main points.

Q MR. COMMISSIONER LIPSETT: Just before you pass from that, Mr.Frawley. Mr. Mercer, I would like to get a little further detail from you on these various headings, as to the figures that you say should be altered and as to the extent of the alteration that that would bring out in your final figure. I think you dealt with depletion first?

A Depletion, yes sir.

Q What was the actual figure for depletion that was written off in that exhibit "290" or Exhibit "255"? Or taken from "255"?

A In "255" I applied the figure of $494,258.61.

Q For depletion?

A For depletion.

Q And that figure is written off before you arrive at this 78½ cents?

A Yes, sir, that is part of the cost.

Q Now in what way is that figure arrived at?

A That is arrived at in an allowance made to the Company by the Income Tax Department of the Dominion Government. It is the net operating profit of the Company. I might qualify that, 25% of the net operating profit of the Company after deducting interest or income from investments.

Q In the Income Tax Act you are allowed to write off 25% of the profit?

A Net operating profits, yes, after deducting such income from bond investments and items of that character.

Q In what way do you say that is incorrect? Is it too little or is it too much?

A That has no direct relation to the capital invested. That has only relationship to the earnings of the Company, or the earnings derived by the Company from its plant, and of course, from the development of its leases.

Q But is the effect of your evidence, Mr. Mercer, that $494,000.00 is not enough to write off for depletion?

A It may not be enough to the extent that we may have an investment figure that we consider should be amortized, a figure of $600,000.00 or $800,000.00 per year.

Q Can you give us the particulars of what, in your opinion, is the figure, the capital figure that you say should have been written off for depletion?

A I cannot do that offhand, Sir. I haven't the figures available in my mind.

Q It may, on what we have before us at the moment, it might be that is too high a figure to write off for depletion just as much as it is too low?

A It might work that way, Sir, yes.

Q Can you give me a figure for the actual money expended in drilling in that particular year?

A In that particular year?

Q Yes?

A I would have to familiarize myself with that figure.

Q I would be glad if you could get that figure?

A I am keeping in mind your request for a memorandum and as soon as I get the time I am certainly going to do that.

Q I would be glad to get that. We have had this general statement thrown out about the Jersey Statements, and while it may be too little and quite possibly on the

other hand it looks a substantial figure to write off, $494,000.00 for depletion in one year. I would be glad to have it worked out in detail, and shown whether it is too little or too much or fair?

A Yes.

Q Now, going to the next figure, the depreciation figure. How much depreciation was written off in arriving at the figures for that year?

A Depreciation on this statement has been generally applied against the various items, as shown, and is not a distinct and separate total. In 1938 I believe the depreciation was in the neighbourhood of the same amount as depletion. I would say approximately it was half a million dollars. I do not know how close that would be, Sir.

Q But approximately?

A It approximated half a million dollars depreciation.

Q THE CHAIRMAN: With depletion?

A No, separate from depletion.

Q Separate from it?

A Yes.

Q MR. COMMISSIONER LIPSETT: So that included in the statement now showing 78½ cents a barrel as the cost of Royalite crude oil, there is approximately $1,000,000.00 written off for depletion and depreciation before that figure is arrived at?

A Yes, and proportion of that has been applied against the cost of producing crude oil, yes sir.

Q I would be very glad, speaking for myself, I would be very glad indeed if we could get that worked out in actual detail, the actual percentage of depreciation

and depletion and any other particulars about these two items?

A Yes.

Q Now I think the next thing you said was interest on investments, that there may be some error?

A Only to the extent of the advisability of including interest on investments as part of costs. You will find some authorities will accept interest on investments in arriving at cost.

Q I do not know that I quite follow what you mean. I would be glad if you would explain it?

A Only to the extent you have a certain amount of money tied up in your capital investment, and as such you take a percentage, 6% of your investment and apply that as part of your cost.

Q That is to say, assuming, just to get it clear in my own mind, assuming the capital was $1,000,000.00?

A Yes.

Q Before you begin to take out the profits, you charge 6% on that million as a cost?

A Yes, as a cost, in order to arrive at the cost.

Q You mean you would have to borrow $1,000,000.00 from a particular bank?

A Quite right, Sir.

Q Were there any other items in addition to those three?

Q THE CHAIRMAN: Did you take interest on investments in here?

A No sir, there is nothing but book entries in these statements referred to as the Jersey Statements.

Q MR. COMMISSIONER LIPSETT: That would not be usual would it, Mr. Mercer, to take interest on investment

unless you actually had to go and borrow the money from the bank, or would it?

A I have seen it used. I have seen interest on investments shown as part of the cost. I will admit, though, there is a divergence of opinion as to whether it is admissible as a cost.

Q Ordinarily if you had to go and borrow the money from a bank......

A You would have interest charged in your costs.

Q Then it would be the true cost in everybody's view? The cost of getting that money? Where it is money just put up as part of the capital is it usual to charge it?

A As I say I have seen it but I only raised that as a point, Sir, of consideration.

THE CHAIRMAN: At the moment it strikes me either it would be an operating cost or it would not. The circumstances that one man had the money in his pocket and another went and had to borrow it would make no difference.

Q MR. COMMISSIONER LIPSETT: Were there any other points where there was a possibility of error that you had in view, Mr. Mercer?

A Only to the extent that by using the revenue basis we may be making a wrong distribution between the subdivisions in a cost statement, because of the volume of revenue of the individual departments.

Q Yes. Well as far as the figures in that Jersey Statement are concerned, your error, or suggested error there was that there was not enough of indirect costs charged to the pipe line. You wanted to put that figure up, I

think, from about 18 to 28% in the pipe line costs.

A That is the difference between the labour ratio basis and the revenue basis.

Q And the Price, Waterhouse basis?

A Yes.

Q I think the Price, Waterhouse figure was around 28% of indirect costs?

A Yes.

Q As against the Jersey Statement of around 18%?

A Yes sir.

Q Is that not correct?

A Those figures are familiar to me.

Q THE CHAIRMAN: You are not sure whether they are correct or not?

A No.

Q MR. COMMISSIONER LIPSETT: The 28% was not accepted, but if it had been, just putting this theoretically, if it had been accepted that would have reduced the cost of crude oil as it appeared in the Jersey Statement would it not? That is to say if more indirect costs were put on the pipe line that would have reduced the cost of a barrel of crude?

A Yes sir.

Q I think in the net result that probably the Jersey Statement figure or something very near it was taken?

A Yes.

Q Both by Mr. Morrison, and I think in the final recommendation that the Commission made?

A I would not know. I have not followed it very closely until the present time, Sir.

Q Assume that approximately the Jersey Statement figure for

the percentage of indirect cost was taken, then that would leave the Jersey Statement correct as far as that distribution of indirect cost was concerned, for the purpose of estimating the price of crude?

A Of crude oil, yes.

Q THE CHAIRMAN: As far as these Jersey Statements go you are the one, are you not, who breaks that up in response to Mr. Commissioner Lipsett's request?

A Yes. Yes, I am going to.

Q Showing whether there may be error or omission?

A Yes. I tried to explain generally some of the larger items that came into my mind now.

Q MR. SHAW: Just one or two questions. Mr. Mercer, I was interested in your statement with regard to these Sterling Pacific wells, 3, 4, 5 and 6. You have an estimated figure for your administration cost of $150,000.00 for a ten year period. That is correct is it not?

A Yes.

Q At least $15,000.00 a year?

A Yes.

Q Now then, I take it, Mr. Mercer, I gathered from what you say there are no figures to substantiate this. It is what you call a considered estimation?

A A considered opinion or estimation, yes.

Q You do not base it upon any particular figures that you have, or experience in connection with similarly situated wells?

A No sir. The only experience we used was the actual experience of our expenditure.

Q With relation to what? To these particular wells or some other wells?

A We anticipated we would spend so much money during the next 10 years.

Q Now these wells, are they Royalite wells at the outset or are they contract wells or what particular variety?

A These individual wells are Royalite wells.

Q And I am told, you can tell me whether I am right or not, that they are situated in the Northern end of the crude oil area, is that right?

A They are situated on the West Half of Section 33, in Township 18.

Q That is in what is called the crude oil area?

A That is the crude oil area.

Q It would be at the Northern extension of that particular crude oil area. Northern and Western perhaps?

A Northern. It could be considered the Northern area, yes.

Q I do not mean the Northern area of Turner Valley?

A No.

Q But the Northern area of the crude oil area?

A I believe though, that wells are being drilled North of this specified area which are producing crude oil.

Q And these have a production which is much greater is it not, than the average production of wells in that area, or can you tell me?

A I do not believe so. We took this as a group of wells that would give an average picture, and the production was taken into consideration. We did not pick a group of wells with small production nor great production.

Q Can you give us an idea of the production of these

particular wells, 3, 4, 5, and 6, the ones you referred to? Have you the figures?

A I have not got the figures. It is noted on the statement, however, Mr. Shaw, that the wells have produced so many barrels of oil up to March 31st.

Q Up to a certain point?

A Yes.

Q But that would not help us as to the daily production unless we knew just the days they had been producing?

A I do not know the last allowable production.

Q You cannot tell what the average production is of this group of wells?

A No, I do not know what the average daily production is.

Q Now, coming to the break-up of the statements to which the Commissioner has referred. There are just one or two things I want to ask you. These Jersey Statements, so-called, are prepared by your office for the information of whom?

A They are prepared originally by our office to enable us to cost the inventory of oils, crude naphtha and crude oil and so on, which we may have on hand at the end of an accounting period.

Q And so every year you figure these up for those particular years and you have it 78 cents plus?

A Yes, one year.

Q And at the end of the year you take your inventories of oil on hand and you say that is worth so much?

A On that memorandum of cost basis.

Q Do you use it for any other basis?

A We have used it in supplying statistical data to the Executive.

Q The Executive. Now who would you refer to by the Executive, the Imperial Oil Company or the Standard Oil of New Jersey or both of them?

A The Imperial Oil Limited when they request it.

Q I gathered from what you said this morning or did I gather it correctly, these statements are prepared twice a year?

A Yes, we close our books twice a year.

Q Then I take it a statement is furnished to your head office at Toronto?

A Yes.

Q A statement such as you have there, Exhibit "255" is furnished half-yearly to your head office in Toronto?

A Exhibit "255" has been in the past. We are not now submitting this exhibit.

Q You mean you are not submitting it now to the Imperial Oil Company?

A To the Imperial Oil Limited.

Q I take it there must be some standard or is there any standard system of accounting for the Imperial Oil Company in its various activities, and your Royalite and other companies here?

A Yes.

Q Or have you insofar as the Royalite is concerned a separate system of your own?

A We have a separate system. We have no separate system of general accounting, no sir.

Q I observe in one of the statements that - a letter produced December 14th, 1938, written to your office here, that they seem to have some difficulty in reconciling the statements made, your statements made

[illegible]

apparently, as far as Income Tax returns are concerned, the published annual statements and the several schedules supporting the returns. Do you know of any effort on the part of the head office to reconcile these statements and having some difficulty in doing it?

A You are referring to the letter of Mr.C. D. Dean?

Q Yes? I only want that reference to it because I am not concerned with the rest of the letter?

A This is a letter which was written by Mr.Dean's department.

Q That is the accounting department at......

A He is the comptroller of Taxation for the Imperial Oil Limited, to us, as the title designates, he is the comptroller of taxation of the Imperial Oil Limited.

Q Yes?

A In the matter of the submission of our Income Tax he raises the question that he was not able to reconcile certain of the figures from the schedules which have been submitted to the Dominion Income Tax Department.

Q He was finding difficulty - I am not concerned with the reasons why - but he was finding difficulty in trying to reconcile the Royalite Statement to its shareholders with the Income Tax return and the schedules that were produced, and he was apparently trying to get some standardized system.

A That is quite right, although he leaves the matter entirely in our hands insofar as the tax is concerned. That is quite understandable to this extent that details of our full accounting is not available to Toronto in the usual form which we submit our information to them. We have a number of sub-accounts in our ledgers under

main classifications. The amount of the main classifications only are submitted to Toronto. The schedules as submitted to the Dominion Income Tax Department take up complete details of our books right from our general ledgers and tie in with the profits.

Q That was the difficulty apparently trying to reconcile those statements and tying one with the other?

A Yes.

Q That may be and probably is a matter of bookkeeping or accountancy. What I want to get at is the fundamental purpose of submitting these statements to the Imperial Oil Company is for their accounting Department is it not?

A Yes. To their accounting department to assist....

MR. NOLAN: What statement is my friend referring to?

MR. SHAW: Exhibit "255".

MR. NOLAN. The Jersey Statements?

MR. SHAW: That is the one we are talking about?

A This Exhibit "255" is only a substantiation to show what value we place on the oil on hand, a figure which is reflected in our balance sheet.

Q A sort of transubstantiation because it is sent across country. In any event, Mr. Mercer, the statement involves a great deal of time and a great deal of effort does it not, in its preparation? At least I judge.....

A No, in preparing this statement in the first instance that is for the purpose I use it for, I might say I prepared this statement in a matter of a few hours.

I have got to prepare it in a matter of a few hours or I hold the whole office organization up.

Q What I was wondering about is - well can you give me a rough idea of your inventories of oil on hand at the expiration of your accounting period?

A There may be three or four thousand barrels of oil.

Q Three or four thousand barrels of oil? So that you say that you want to ascertain the exact cost figures for inventory purposes of those three or four thousand barrels of oil when you make this statement?

A We do not anticipate making an exact cost figure. It is a cost index figure to give us an idea.

Q Is not that the basis on which you make up your inventories for head office?

A Yes. But not in any way an exact cost. We have never considered it as such.

Q Apparently the Imperial Oil's head office must be satisfied that it is the exact cost, otherwise they would not accept it?

A They have only accepted it in the spirit in which it is made up and submitted, that it is an index to guide them.

Q I suppose their purpose in getting this guide - do they use it in their statements do you know?

A They have requested and I presume used statements such as Exhibit "286".

Q It has been used.....

A I presume. We have been asked to submit that information to them and I presume they use that information.

Q They will use it for the purposes of their accounting purposes and to their shareholders I suppose?

A They will use it as an index and guide.

Q Is it used in your manufacturing department'

A I would not know.

Q You do not know? You would not be surprised, I suppose, if it was?

A I still do not know, Mr. Shaw.

Q Now, how long have these statements, over the course of time, have these statements been regularly forwarded to the Imperial Oil Company for their purposes?

A Which statements are you referring to?

Q I am referring to the Jersey Statements, the same ones we have been discussing?

A As far as the Jersey Statement is concerned it is only a substantiation of a figure appearing on our balance sheet. I do not know whether the Imperial Oil Limited use that figure for any informative purposes at all. Although with the other exhibit, the information they specifically ask for and the basis of which is the Jersey Statement......

Q For how many years have you prepared, Mr. Mercer, this statement for the Imperial Oil Company?

A The Jersey Statement?

Q Yes?

A Since 1933.

Q Since 1933? So that in any event you have been furnishing them this statement during that period which they use for whatever purpose they see fit? That is about your evidence?

A Yes sir.

Q Now, just one other matter, Mr. Mercer. You have spoken about the depletion allowance. Who figures the depletion

allowance? Who fixes the amount of that depletion allowance?

A The Dominion Government Minister at his discretion.

(Go to Page 8872A).

Q Quite right, and do you know as a matter of fact that the allowance which is ordinarily and regularly made for oil companies?

A It is not the ordinary allowance made to oil companies.

Q Then is it the experience of the Royalite Oil Company that they secured a 25% depletion from the Minister?

A That we secured?

Q That you secured?

A Yes, we secured a 25% depletion of the net operating profits only.

Q I want to make it clear, the depletion allowance is fixed by the Minister?

A Yes.

Q And he fixes that from year to year, or do you go on a fixed figure?

A It is a fixed figure.

Q Now with regard to the depreciation allowance, who fixes that?

A The Minister at his discretion.

Q I mean you fix it and he can change it if he wants to, is that not the situation?

A They have advised the amount of depreciation they will allow as a deduction.

Q And what is the amount of that depreciation allowance?

A It varies according to the class of plants or buildings in operation.

Q Well you know the class of buildings in operation in the Royalite Oil Company, what is the depreciation allowance which the Minister allows?

A We take and book as depreciation at rates of 10 and 15%. In the case, I may qualify that now, in the case of automobile

equipment we take a larger allowance.

Q So that you have not any figure which would indicate the average depreciation allowance?

A No sir.

MR. SHAW: I think that is all, Mr. Chairman.

TO MR. FRAWLEY:

Q Mr. Mercer, following up with what Mr. Shaw has been asking you about, you told us the other day about Mr. C. H. Mullinger, who is he?

A He is the Accountant for the Imperial Oil.

Q Accountant for the Imperial Oil?

A I always understood that he was the Accountant.

Q I am wondering about that, perhaps Mr. Nolan can tell us, there is nothing, I do not want to find meanings where there are no meanings, but he simply uses the letterhead, 56 Church Street, Toronto, he doesn't appear to be of the Imperial Oil, I wonder if you can tell us, Mr. Nolan, who he is?

Q MAJOR LIPSETT: Can you give us the figure, Mr. Mercer, of the net operating profits on which this depletion was based?

A For 1938?

Q Yes?

A I would have to advise myself on that also. They are worked out in Schedule form at the time I present our Income Tax return.

Q Would you get that?

A Yes I will.

Q You might make a note of that please?

A Yes.

MR. FRAWLEY: All right, that is all. Now Mr. Chairman, it was at this stage that we had completed for the time being only of course the question of cost of production, this arose out of Mr. Plotkins' request for further correspondence and statements to be obtained from the Royalite Oil Company and we have done that and Mr. Mercer has been on the stand now for a considerable time producing these further documents and submitting to cross-examination about them. I then propose to go on with Mr. McGrath who will submit his two further statements of refinery spread and costs of, statement of capital invested in the Province, and which will complete Mr. McGrath's evidence. I was hopeful he would be able to go on at 2 o'clock. I may say that those statements have caused him a great deal of concern, the preparation of these statements, and he advised me personally at the noon adjournment at half-past twelve that it would be quite impossible for him to go on this afternoon but undoubtedly he would go on at 10:30 in the morning and continue on without any further breaks until he had completed all of his statements and all of his evidence. That being so there is nothing else to go on with and I feel that we are warranted now, Mr. Chairman, in applying for an adjournment until Mr. McGrath can come along and I would ask that that be so.

THE CHAIRMAN: You are deferring further examination of Mr. Plotkins, are you?

MR. FRAWLEY: As to costs?

THE CHAIRMAN: Well Mr. Nolan has never cross-examined and he has an undoubted right to.

MR. FRAWLEY: Oh yes, that is true. I had com-

pleted my cross-examination of Mr. Plotkins.

THE CHAIRMAN: Yes but Mr. Nolan had not.

MR. FRAWLEY: Yes, I am aware of that. There was a long statement----

THE CHAIRMAN: I am not suggesting what your order should be. If you want to defer the cross-examination of Mr. Plotkins and Mr. Nolan has no objection----

MR. FRAWLEY: I would only say this, sir, we have started now----

THE CHAIRMAN: You may be quite right if I might interrupt, but I do not want it lost sight of that Mr. Nolan has the right to cross-examine the witness and will be allowed to exercise that right. As to when I suppose it matters not to anyone. Your preference is not to embark upon that until after you have gone on with Mr. McGrath.

MR. FRAWLEY: Yes, quite so and then with Mr. Halverson, and we are into quite a long stretch of evidence then.

THE CHAIRMAN: So long as it is agreeable to everyone, to Mr. Shaw----

MR. SHAW: No objection.

THE CHAIRMAN: And Mr. Nolan.

MR. NOLAN: I have no objection.

THE CHAIRMAN: Then we will adjourn until to-morrow morning.

(The Inquiry was here adjourned to be resumed at 10:30 A.M. June 13th.)

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The Province of Alberta

IN THE MATTER OF THE PUBLIC INQUIRIES ACT

—and—

IN THE MATTER OF a Commission, dated the 12th day of October, A.D. 1938, to inquire into matters connected with Petroleum and Petroleum Products

Commissioners:

The Honourable MR. JUSTICE McGILLIVRAY
(Chairman)

—and—

L. R. LIPSETT, ESQ.

Session:

CALGARY, Alberta June 13th, 1939

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JAMES MCGRATH, having been recalled, examined by Mr. Frawley, said:

Q Good morning, Mr. McGrath?

A Good morning, Mr. Frawley.

Q What have you to offer us this morning?

A First of all, I would like to file some schedules which have been requested.

Q Requested up to now?

A Yes.

Q Thank you.

A When I filed Exhibit "281", Schedule 2 in that Exhibit, shows the marketing cost for the year 1938, and as requested by the Commission Counsel, he requested that more details be given of those costs, and upon reviewing same with Mr. Cottle, it was suggested that we hand in a new Exhibit in substitution for this, giving more details. The Accounting Department apparently in preparing the copies in the book compressed the items or compressed the expenses into a very few items, and it was felt that it would facilitate a proper investigation of those costs, that these detailed costs be filed.

Q Then you are taking out Schedule 2?

A That is right.

Q Marketing Costs, both Sheet "a" and Sheet "b", are you?

A Yes.

Q And you are substituting one sheet or two sheets?

A Three sheets, Mr. Frawley.

MR. FRAWLEY: Do you see that, Mr. Chairman, it is Exhibit "281" now.

THE CHAIRMAN: Yes. Schedule 1?

A Schedule 2, Sir.

Q MAJOR LIPSETT: Of Exhibit "281"?

MR. FRAWLEY: Yes, it is called "Marketing Costs", and there are two sheets, Sheet "a" and Sheet "b", then you are going to substitute three sheets?

A Three sheets, "a", "b", and "c".

MR. FRAWLEY: And this will be Exhibit "300".

DOCUMENTS PRODUCED BY THE WITNESS HERE MARKED AS EXHIBIT "300"

Q Then Exhibit "300" consists of three sheets as substituted for Schedule 2, consisting of two sheets, in Exhibit "281"?

A Yes.

THE CHAIRMAN: "a" and "b"?

MR. FRAWLEY: Yes, and we will now have "a" and "b" and "c". It comes out, of course, to the same figure of $1,025,448.90. We will not be able to discuss that with you now, Mr. McGrath, probably, so would you go on with something else?

A There was another statement, Mr. Frawley; in dealing with the S-309, that was the large Marketing Costs Statement, your requested it be broken down into a column of statements showing how that money was spent.

Q That form S-309 was marked as Exhibit "282". Now you are filing this statement entitled "Schedule 2, Marketing Costs", which, as I understand, has the same information as contained in Exhibit "282", form S-309, except this new Exhibit is in columnar form?

A That is right.

DOCUMENTS PRODUCED HERE MARKED AS EXHIBIT "301"

Q THE CHAIRMAN: It covers the whole Exhibit "282", does it, in different form?

[illegible]

[illegible]

[illegible] good [illegible]

[illegible]

MR. FRAWLEY: It has everything that is in S-309 in different form?

A That is right.

Q And as Mr. Cottle asked me to point out, it ties in with the exhibit you have just filed, Exhibit "300"?

A Exhibit "300", that is right.

Q Then it is understood, also, that Mr. Halverson, when he is giving evidence will submit us supplementary evidence in further explanation of the figures in Exhibit "301"?

A That is my understanding.

Q All right?

A The next statement is the Product Specifications of the Calgary Refinery, Mr.Frawley requested that?

Q Yes?

A Now I am filing statements on the specifications of gasolines, kerosene and fuel oil; do you want asphalt and things of that nature?

Q No, it is not necessary, Mr. McGrath.

MR. FRAWLEY: This is a statement, "Calgary Refinery Product Specifications, being the specifications of Imperial Naphtha, Esso Gasoline, 3 Star Imperial Gasoline, Premier Gasoline, Acto Gasoline, Turner Valley Casing Head, Tractor Distillate", those are all of the products which are marketed out of the Calgary Refinery?

A Yes, that is the gasoline products.

Q Motor fuels?

A Yes.

STATEMENT PRODUCED HERE
MARKED AS EXHIBIT "302".

J. McGrath

Q THE CHAIRMAN: That is a statement of the specifications of the motor fuels marketed out of the Calgary refinery?
A Yes.
Q MR. FRAWLEY: Now the next one, Mr. McGrath, is a statement "Product Specifications" for kerosenes and fuel oils, it is really just a continuation of Exhibit "302"?
A Yes.
Q You could have put them all on one sheet if you could have got them on, I take it?
A Yes.

DOCUMENT PRODUCED HERE
MARKED AS EXHIBIT "303"

Q This is called "Product Specifications, Kerosenes and Fuel Oils", are these motor fuels, these kerosenes and fuel oils?
A It is burning oils.
Q Now, Mr. McGrath, just dealing with these two Exhibits, Exhibit "302" and Exhibit "303", I did not expect these until Mr. Halverson went in the box, and I would like to ask you a couple of questions about them, if you can answer; these products on Exhibit "302", take the gasolines, for instance, Esso Gasoline, that is the gasoline which is marketed by Imperial Oil Limited as Ethyl Gasoline?
A That is correct.
Q Then the gasoline which is marketed by the North Star Oil Company as Ethyl Gasoline, you have not the specifications for that?
A No, I have not.
Q Nor for any of the gasolines which you make for your jobbers, under your jobbers' contracts?

[illegible]

A That is correct, Mr. Frawley.

Q It was expected they would be filed and that is why I did not expect we would have it until Mr. Halverson went on. Would you have a note made to supply us with those jobbers' specifications?

A I will.

Q All right, Now, then, Mr. McGrath, you have something else?

A In Exhibit "280", Schedule 3, Manufacturing Costs, Mr. Frawley requested more detail of some of the items shown in this schedule and I have here a statement giving considerable details of them.

Q The one statement covers details of various items?

A That is right.

MR. FRAWLEY: This is a statement, Mr. Chairman, entitled "Calgary Refinery, Manufacturing Costs, Year 1938", and you say that it breaks down a number of the items in Schedule 3 of Exhibit "280"?

A That is right, Sir.

(DOCUMENT PRODUCED HERE MARKED AS EXHIBIT "304").

THE CHAIRMAN: Schedule what, in Exhibit "280"?

MR. FRAWLEY: Schedule 3, in Exhibit "280".

Q MR. FRAWLEY: All right, Mr. McGrath, I will just defer any questions which might arise out of that. Have you anything else?

A And on the same Exhibit there was an item of "Miscellaneous Income" which you asked for details of, Mr. Frawley, $36,321.97 and I have that.

Q Yes, this statement, sir, is a breakdown of the items "Miscellaneous Revenue" in Schedule 3 of Exhibit "280"?

STATEMENT PRODUCED HERE MARKED AS EXHIBIT "305".

THE CHAIRMAN: I thought Exhibit "304" was giving details of Schedule 3 of Exhibit "280"?

MR. FRAWLEY: Of certain items. This is a special sheet with reference to one item, it is the last item "Miscellaneous Revenue", in red, $36,321.97?

Q MR. FRAWLEY: Yes, Mr. McGrath?

A The next is "Administration and General Expense" on Schedule 3 of Exhibit "280".

Q A breakdown of that item?

A A breakdown of that item.

Q A breakdown of the item $67,973.05 in Schedule 3 of Exhibit "280"?

A Yes.

Q THE CHAIRMAN: Did you say administration or general expense?

A Administration and general expense.

MR. FRAWLEY: And this is called "Statement of Refinery General Administration, Year 1938, Applicable to the Calgary Refinery", and it refers to Schedule 3, Exhibit "280".

(DOCUMENT PRODUCED HERE MARKED AS EXHIBIT "306")

(Page 8882 follows)

Q Yes?

A I have another statement showing the detail of the administration and general expense on Schedule 2 of Exhibit "281".

Q Schedule 2. Do you want us to use the new exhibit?

A That is correct.

Q Exhibit "300"?

A Yes, "300".

Q You say what you are now producing is what?

A This is a statement of Marketing, General and Administration Expense, the detail of it.

Q THE CHAIRMAN: The details of what?

MR. FRAWLEY: Details of the item General and Administration Expense appearing on Sheet B of Schedule 2 of the new Exhibit "300".

THE CHAIRMAN: Schedule?

MR. FRAWLEY: Schedule 2 of Exhibit "300". Of course that is "300". "300" is Schedule 2, The figure is $86,768.66.

A No, there is some down here too, on the next page. There is some in there too, Jobbers' Expense. There is some in there.

Q It is a breakdown in any event of all of the General and Administration appearing in this Exhibit "300"?

A That is correct.

DOCUMENT IN QUESTION IS NOW MARKED EXHIBIT "307".

MR. FRAWLEY: It is called, to distinguish it, it is called Statement of Marketing, General and Administration, Year 1938. That is the new Exhibit "307".

Q Mr. McGrath, if you will look at these two exhibits "300" and "307"?

A Yes.

Q Mr. Cottle tells me now that the two do not automatically do not tie in. We will have to have some further links, won't we?

A On Page B of Schedule 2 there is the sum of $86,768.66.

Q Yes?

A Then on Page C at the bottom there is Jobbers' Expense $3,754.10?

Q Yes?

A Now most of that Jobbers' Expense is administration and General Expense.

Q But it is not all?

A No. It is within a few hundred dollars. I think the majority of that is......

Q I do not know how much or how important it is to Mr. Cottle, or how much trouble it is to you, but if we could have a break-down of the $3,754.10 that would do it would it not?

A Yes, that would do it.

Q That would tie it in?

A Yes, that would tie it in.

Q If you will give us a break-down of that figure?

A Yes.

Q Thanks very much. Now what is next?

Q MR. COMMISSIONER LIPSETT: Mr. McGrath, could you tell me, I did not follow, where that $3,000.00 is that makes up the difference between the $86,000.00 and the $89,000.00?

A On the bottom of the last sheet C.

Q MR. FRAWLEY: Mr. McGrath, before you go on with anything else, Mr. Cottle draws to my attention the fact there is one outstanding statement, a break-down in connection with the throughput at Regina. Do you remember?

A The throughput at Regina I gave that to Mr. Lipsett.

MR. COMMISSIONER LIPSETT: The throughput of the Regina Refinery in 1938 and also the capacity. Did I get those?

A Yes sir.

MR. FRAWLEY: Mr.Cottle will tell you what it is he wants.

MR. COTTLE: It is a statement showing the effect of the change in the economic line between Sarnia and Regina at various prices of crude. You read some figures into the record some time ago running from $1.15 tl $1.40 for Turner Valley crude?

A Yes.

Q As I recall it Mr.Frawley gave you a rough schedule which I had made asking you to extend it to $1.00 and put it in the form of an exhibit?

A That is overlooked.

Q MR. FRAWLEY: This Exhibit "283" which is filed is complete?

A Yes.

Q But only goes to $1.15?

A Yes.

MR. FRAWLEY: What you had in mind is that should be run down to $1.00?

MR. COTTLE: Yes, with the correct figures for Calgary. These are merely assumed figures

on my part.

MR. NOLAN: My memory, Mr. Commissioner Lipsett, is that the crude run at Regina in 1938 was 5,363 barrels per day, and that the capacity at Regina was given as between 6100 and 6500, with the explanation by Mr. McGrath that it could not run to the full 6500 capacity every day.

A That is right, Sir.

Q THE CHAirman: That was not in Exhibit form was it?

A No, but it could be put in one.

Q MR. FRAWLEY: That again is a different thing. That is something else?

A Yes, that is a different thing.

MR. NOLAN: From what?

MR. FRAWLEY: From what I am asking Mr. McGrath to do now. All right.

MR. COMMISSIONER LIPSETT: Mr. Frawley, just to get these exhibits together. Exhibit "281" is connected with Exhibit "302", "301" and "300", and "307", is that right?

Q MR. FRAWLEY: Have you got those exhibits there?

A Yes.

Q Tie them in?

MR. COMMISSIONER LIPSETT: Tie "281" and "280" separately if you could.

A Starting with "300". Exhibit "300" refers to Schedule 2 in Exhibit "281". Exhibit "301" refers to, what is that exhibit?

MR. NOLAN: Exhibit "282".

A Exhibit "302" and "303" were the specifications that we have not covered before. Exhibit "304" covers the details of the items in Schedule 3 of Exhibit "280".

Q MR. FRAWLEY: Exhibit"280"?

A Yes sir. Exhibit "305" covers details of the miscellaneous revenue shown on Schedule 3 of Exhibit "280". Exhibit "306" shows the details of the Administration and General Expense showing in Schedule 3 of Exhibit "280". Exhibit "307" is the details of the Administration and General Expense shown on Exhibit "300".

MR. NOLAN: No, shown on Sheet B, Sheet 2 of Exhibit "300".

MR. COMMISSIONER LIPSETT: "307" goes back to Exhibit "281"?

A Yes, that is right.

MR. NOLAN: It does not, Sir.

THE CHAIRMAN: It goes to "300" which in turn goes to "281".

MR.NOLAN: For the sake of clarity we must look to exhibit "300" to see that "307" is a break-down of the Administration and General Expense.

MR. FRAWLEY: Yes. All right, Mr. McGrath, what is next?

A In Exhibit "280" we filed details of Income and Expense for the Calgary Refinery and the territory supplied by the Calgary Refinery. That embraces both manufacturing and marketing operations in that territory.

Q Yes?

A It has been suggested that we show the refining picture, the Calgary Refining picture separate from the marketing

picture. As we do not have refinery billing prices between the refinery and the marketing department we have used the jobbers' tank car prices for the year 1938 to divide the marketing and manufacturing operations. In other words, we have assumed that all the products sold, or produced, were sold at the jobbing prices.

Q Just go back half a second. You said you are now doing this to show, your expression was, the true Calgary Refining picture?

A The refining picture by itself.

Q By itself?

A Yes.

Q To what extent was that not done in Exhibit "280", that showed the Calgary Refinery?

A Yes, but that was for the Calgary Refinery embracing the territory supplied by the Calgary Refinery, both marketing and refining. This deals with refining only.

Q This is what we have been commonly calling here the spread statement,

A What you referred to as the spread statement.
I thought perhaps there should be an exact description of that for the Commission?

A Yes.

Q What precisely does this spread statement.....

THE CHAIRMAN: The spread statement is what number?

MR. FRAWLEY: This is the thing. This is it which he is going to introduce now.

Q What precisely is the object of the spread statement?

What did it seek to do?

A To show the manufacturing picture alone, that is without the marketing picture.

Q In other words, show what you did in the refinery assuming you sold it all in tank cars at the refinery door to the marketing department?

A Well not necessarily to the marketing department, but to the jobbers and marketing.

Q To all?

A Yes, to all.

Q You did actually do that with your jobbers?

A Yes.

Q You are now assuming you did that to your marketing department?

A That is right.

Q Treating them as one more jobber?

A Yes.

Q You are going to show what the Company's experience was putting it on that basis?

A That is right.

Q As to refining?

A That is correct.

Q And that is what this statement does?

A Correct. These statements are based on assumptions, that is assuming we did sell at the tank car price to the marketing department.

Q That is the basic assumption?

A Yes.

Q Underlying it all, of course?

A Yes. It is assumed the total production of the refinery was sold on that basis.

James McGrath.

Q When you say presuming you sold to your marketing department as a jobber, there is some slight variation in the prices that you do sell to jobbers and have you picked out one of them?

A No, it is the average jobbers' price for the year 1938 adjusted for the reduction in selling price as of June 1938.

Q You used the average realization from jobbers in the year 1938 and doing what, adjusting.....

A Adjusting those prices for the effect of the reduction in selling price on June 26th as shown in Schedule 6 of Exhibit "280".

Q You are referring to Schedule 6 in Exhibit "280" for what purpose, Mr. McGrath?

A I said that we used the average jobbers' price for the year 1938 and adjusted that average price for the effect of the price reduction on June 26th, 1938, as shown on Schedule 6 of Exhibit "280".

Q Just looking at Schedule 6 in Exhibit "280", there is a price per gallon after adjustment from jobbers of 11.51 cents?

A No, that is before freight, Mr.Frawley. The price adjustment is the difference between 11.93 and 11.51, or 42 points.

Q The price adjustment is the difference between 11.93?

A 11.93 and 11.51.

Q If that is the adjustment why didn't you use....

A These figures shown here, Mr.Frawley, are before freight has been deducted.

Q 11.51 was the basic figure?

A That is the starting point and then there is freight.

James McGrath.

Q You use the 11.51 and made the adjustment for freight to take it back to the refinery door?

A That is right.

Q All right. This is a statement merely called Refinery Production?

A It is in three parts.

Q Three sheets?

A Yes.

Q Each sheet is called differently?

A Yes.

Q The first sheet is called Refinery Production; the second sheet Sales and Gross Income Less Freight, Sales Tax and Packages, 1938, and the third sheet is called Refinery Profit and production. Between jobbers' prices and cost of crude and absorption naphtha?

A That is right.

DOCUMENTS IN QUESTION ARE NOW MARKED EXHIBIT "308".

THE CHAIRMAN: You have three sheets, one refinery production?

MR. FRAWLEY: The second sheet Sales and Gross Income Less Freight, Sales Tax and Packages, year 1938. The third sheet Refinery Profit and Production between Jobbers' prices and cost of crude and absorption naphtha. That is the description of it.

THE CHAIRMAN: Better make those sheets (a), (b) and (c) hadn't you?

Q MR. FRAWLEY: You are putting them in. Have they got a separate existence?

A The statements are related.

Q It looked to me that the last sheet was a summary?

A It may be dealt with separately if you desire.

THE CHAIRMAN: If they are to be talked about separately mark them separately. If they are not, all right.

MR. FRAWLEY: 308. The first sheet will be "308a".

THE CHAIRMAN: That is all right.

MR. FRAWLEY: And "308b" and "308c".

Q MR. COMMISSIONER LIPSETT: Do these tie in with Exhibit "280"?

A Yes sir. And incidentally, Mr. Lipsett, you requested me for a reconciliation of the gallons in "280". This here reconciles the gallons. Now, Mr.Frawley, how much detail do you wish me to go into on these statements? There is an awful lot of figures here......

Q MR. FRAWLEY: Of course, as you are aware this has been placed before Mr. Cottle and Dr, Brown this minute for the first time?

A Yes.

Q So I am perfectly helpless. I am simply in their hands. I have not any idea. This is, of course, an exceedngly vital statement. It is the one you have been working on for so long. I am afraid I cannot be of any assistance either to you or to the Commission at this stage. I would suggest you start and tell us all you possibly can about it. The only other alternative is for us to go away and study it and come back?

A I will tell you what I will do, if it is agreeable I will go along with my description, and if there is not enough detail you can stop me and I will go into more

detail on the subject.

Q Fine.

THE CHAIRMAN: I am just wondering if you should not, whether we do or not, but if you should not understand these various statements, with the advice of your expert assistants before you even hear the witness discuss them. I am just thinking of expedition in the end, and a clear understanding in the end, Mr. Nolan.

MR. NOLAN: Yes, I know what you mean, Sir.

A May I say I did not intend, in my explanation, to condense the statement to the point that it is not understood. What I mean, in referring to each individual figure I had no idea of condensing it to the point......

MR. NOLAN: The Chairman is suggesting that perhaps any description of any kind might be futile until we know what we are describing.

MR. FRAWLEY: Mr. McGrath knows what he is describing. He is quite familiar with it. I, of course, know nothing about it. Mr. Cottle and Mr. Brown are just looking at it for the first time. Mr. Cottle suggests that you proceed to describe it. The only point is I cannot be of any assistance to the Commission in asking pertinent questions on it. I would have to leave it to Mr. McGrath. I do not mind myself. But I cannot try to understand it until these men have seen it.

THE CHAIRMAN: Well, what I am coming at, Mr. Frawley, and if you think it would be of interest at this time, the question is the best way to do it.

MR. FRAWLEY; Yes.

THE CHAIRMAN: If Mr. McGrath proceeds to discuss these statements at this time, your experts are wholly unfamiliar with them until they have had an opportunity of studying them. Now, when Mr. McGrath makes some statement with respect to some figure there, if they have considered it, they will have instructed you, so that you can ask intelligent questions about it, right then, so my thought was, Mr. Frawley, whatever you may think about it........

MR. FRAWLEY: I think perhaps there is some value in that.

Q MR. FRAWLEY: Mr. McGrath, you would probably have one more statement, that is a statement of capital investment which has to be read and considered in conjunction with your spread statement?

A Yes, I have several statements here in conjunction with them.

Q Then certainly file all your statements, and for my part I would be very glad to accept the Chairman's suggestion, to go away and look at them.

THE CHAIRMAN: I think in the end, not only before you cross-examine, but when you hear the witness in a discussion of the items, that you or the experts may find that some of them are quite clear and need not to be examined about; equally they may have a number of figures that they want cleared up.

MR. FRAWLEY: Yes.

THE CHAIRMAN: Well surely they should have an opportunity of studying the statements and deciding on what they do want to know about them, in addition to anything which Mr. McGrath volunteers.

MR. FRAWLEY: I think so. You see the business of Mr. Cottle now in trying to check in his working papers, would be a difficult thing to do here, that might better be done in his own office or elsewhere.

THE CHAIRMAN: Yes.

Q MR. FRAWLEY: Will you continue to file everything you have got?

A Yes, I will, Mr. Frawley.

MR. FRAWLEY: And then we will go ~~away~~ and look at them.

THE CHAIRMAN: Ultimately, so far as I am concerned, with the help of all the experts we have, including Mr. McGrath, and any notes which Mr. Nolan may have, I would like to find that it, instead of being a mass of figures and statements, that it results itself into some simple proposition which may be put into words.

MR. NOLAN: It would, and I would like to make it clear, Sir, that this statement which Mr. Cottle has not seen, as my learned friend says, it is right that Mr. Cottle has not seen it, but it is the slow growth of discussions which have taken place, this is what has emerged in its final form.

MR. FRAWLEY: I think there are some off-shoots on the growth.

MR. NOLAN: Well I do not know what that means.

THE CHAIRMAN: I am sure that Mr. Frawley would not start anything or make any statement which would have a sinister meaning.

MR. FRAWLEY: No, I might have up to a few days ago, but never anything any more.

Q MR. FRAWLEY: Well, what else have we got now?

A We have a statement here similar to Exhibit "308", "a", "b" and "c".

Q Similar to "308" (c)?

A Yes, but it is, I might term, a theoretical figure in this way, in processing crude to our refinery we have at the start of the first of the year a certain quantity of unfinished stocks on hand, and at the end of the year we end up with a certain number of stocks, a certain quantity of unfinished stocks on hand; those stocks are a different quality, and that sort of thing, so I have prepared a statement to show the approximate figure of finishing up those stocks, that is bringing it into the finished products picture.

Q Very well.

A In other words, we start with say 6,000,000 gallons of unfinished stock at the beginning of the year, we run 69,000,000 of crude oil, and we end up with 7,000,000 of unfinished stocks on hand, so in our products at the end of the year we have the finished products from the 6,000,000 that we started with and which we have completed, and we have that also which we process during the year, and we have left 7,000,000 gallons of unfinished stock, and what I have tried to do here is to estimate the production, adding in the inventory at the end of the year

on an estimated basis so as to get the whole picture.

Q Of the twelve months?

A Yes.

MR. TRAWLEY: This is a statement entitled "Refinery Spread Between Jobbers' Prices and Cost of Crude and Absorption Naphtha, After Conversion of Unfinished Stocks", and that will be the next Exhibit.

(STATEMENT PRODUCED HERE MARKED EXHIBIT "309")

Q Yes?

A In the study of refinery spreads which finally result in refinery profits, I felt the Commission would be interested in a statement showing the manufacturing costs of the Calgary refinery over a period of years, to show what effect, or to demonstrate what effect volume has on the manufacturing costs, and I would like to file.........

Q The statement you now produce does that?

A Yes, it shows the run each year from 1930 to 1938 inclusive, the amount of money spent in manufacturing costs for those years, and the cost per barrel for each year, and it varies from 42¢ to 84¢ per barrel with an average for the nine years of 63¢ per barrel.

Q This is a statement merely entitled "Calgary Refinery", and just describe it, Mr. McGrath.

Q THE CHAIRMAN: To show the effect of volume?

A The effect of volume on refinery costs.

Q MR. TRAWLEY: Between the years 1930 and 1938 inclusive, and showing the average for the nine years.

(DOCUMENT PRODUCED HERE MARKED EXHIBIT "310")

Mr. McGrath

Q MR. FRAWLEY: Anything else, Mr. McGrath?
A The next Exhibit is the Assets and Liabilities of the Calgary refinery.
Q As of a particular date?
A As of December 31st, 1938.
Q This statement, "Calgary Refinery, Assets and Liabilities", the date is not shown, but it is?
A As of December 31st, 1938.

(DOCUMENT PRODUCED HERE MARKED AS EXHIBIT 311)

Q Yes?
A I would like to discuss this statement for a moment, Mr. Frawley.
Q Yes, the statement, Exhibit "311"?
A Yes, the statement, Exhibit "311"; the statement shows that the cash on hand as at December 31st, 1938, of the Calgary refinery, is $45,177.00, and the Accounts Receivable was $28,238.88; other Accounts Receivable, $437.64; Inventories of Crude and Products on Hand at Cost, $976,15?.28; Inventories of Material and Supplies at Cost, $114,303.60; Prepaid and Deferred Charges, $2,211.13. The next item is "Fixed Assets", fixed capital assets........
Q That is all the refinery assets?
A That is the refinery assets, the Calgary refinery assets. Now we show the cost, it is shown in the statement, the cost of the Calgary refinery equipment as $5,289,267.42; now there may be comparisons made between the cost of our plant at Calgary and other plants, I would just like to leave this suggestion with the Commission, and that is that you cannot judge, you cannot perhaps relate the cost of plants to the

J. McGrath

rated capacity of the plant, and what I mean by that is this, our Calgary refinery operates, first of all, our sales from the Calgary refinery are made in the following ratios, about 70% of the sales are made in six months and 30% in the remaining six months; we operate the Calgary refinery at an even rate throughout the year and store the products to meet the demand in the six months during the summer time, consequently we carry a large tankage. Now, when you are talking about the rated capacity, you may have two refineries of the same rated capacity per day through the sales of refined products, and the one with tankage can operate at that rated capacity throughout the year, while the other can only operate at the rated capacity so long as the market takes up their production. Have I made myself clear?

Q Yes.

A So in comparing the capital investment, that is a thing which should be considered.

Q THE CHAIRMAN: Have you figures to show what this tankage amounts to?

A The tankage amounts to approximately 1,000,000, sir, a million barrels tankage.

Q MR. [illegible]: Perhaps the Chairman means you could give us the breakdown, and perhaps you intended to give us some breakdown of that item of $5,289,268.42?

A I was going to come to that later.

Q And then you say that the amount of tankage........

J. McGrath

A I have a suggestion to make on that, if you would let me, Mr. Frawley.

Q All right?

A Have I made myself clear on the two types of refineries, Mr. Chairman?

THE CHAIRMAN: Oh, I think so.

A Yes.

Q THE CHAIRMAN; But if I am understanding you aright, the difference to which you point is extra tankage?

A Yes, yes, and probably some other equipment, I do not know.

Q Oh yes.

A But there are two different types of operation, one evenly throughout the year with tankage and the other is according to seasonable demands and shut down during the periods when the demand is low, two different types. Our plant in Calgary is the type that operates throughout the year and stores the product to meet the peak in the summer time.

Q MR. FRAWLEY: This is a figure which is taken from the books?

A That is right.

Q Just a build-up, you might say, of the inventories for equipment purchased?

A That is the cost of the equipment purchased, that is right. Now, this plant of ours was built in 1923, and since that time of course there have been a lot of changes made in it; additions have been made during that period; however the cost as I mentioned before of the equipment is $5,289,268.42.

J. McGrath

Q THE CHAIRMAN: This statement, Exhibit "311", is
at this date, is it?

A December 31st, 1938, sir.

Q Oh yes, I have a note of that, thank you.

A Yes. Now that plant has been depreciated over the
year.

Q Now, just a minute, December 31st, 1938, oh yes, that
is the end of last year?

A Yes.

Q Yes?

A In regard to the fact that part of the equipment is
old, that same equipment has some commercial value
today. Now, this subject is one of considerable
magnitude and I have a suggestion to make; we have
shown on this statement a reserve for depreciation
as of December 31st, 1938, of $3,444,126.35, leaving
the net depreciated value of that plant of $1,845,142.17;
now the purpose of this statement is to show the capital
employed in the Calgary refinery, presumably to base
their return on. Now, I have a suggestion to make
in this connection, and I think it would probably
facilitate the operations of this Commission, and
that is this, I have with me the details of all the
costs of this equipment in making up the $5,289,268.42
and I would suggest that Dr. Brown in his wide
experience and Mr. Cottle review these figures with
myself and see if we can come to some fair value
for that equipment, fair to ourselves and fair to the
Commission. It would not take a great deal of time,
and as a matter of fact, I think it would save a
great deal of time in this hearing. That is just
a suggestion, sir.

MR. FRAWLEY: There is no use of wasting time at this moment.

THE CHAIRMAN: Of course, we can only suggest that you discuss that amongst yourselves.

MR. FRAWLEY: Yes, it is a question......

THE CHAIRMAN: We are only anxious to save time and facilitate everybody in getting the evidence in.

WITNESS: Yes.

THE CHAIRMAN: If it can be explored that way as well as any other, all right, and if it cannot be, all right. It is a question of Mr. Nolan with yourself and the others discussing I think which way in your judgment will best serve to help us.

MR. NOLAN: As I understand it, sir, there is a mass of figures behind the coststhat have been put upon these fixed assets.

THE CHAIRMAN: Yes.

MR. NOLAN: Now if there is any short way of arriving anywhere, it is to be preferred, because from my experience and my discussions with these gentlemen, it will take Mr. McGrath some time to go into these items that make up this figure of $5,289,268.42.

WITNESS: That is right.

Q MR. NOLAN: It would take some time, would it?

A Yes.

Q A long time?

A Yes, it would.

MR. FRAWLEY: We do not know, we will have to give that whole thing some consideration.

THE CHAIRMAN: Yes. It looks very much as though you would have the afternoon free.

MR. FRAWLEY: Yes, we certainly will.

THE CHAIRMAN: And that being so, you can discuss it with each other, and we must, in the end be guided by you, Mr. Frawley, I mean for the production of the evidence, but if there is any way in which there is a short-cut to an understanding of this, we welcome it, of course, as I am sure you will.

MR. FRAWLEY: Yes, we will have to study it.

THE CHAIRMAN: On the other hand, if you see some objection to the suggestion put forward by Mr. McGrath, you will naturally not adopt it, but I do suggest that it be given some consideration.

MR. NOLAN: And I hope you do not feel that we have not been making some headway, because we have done more this morning than we have done for a long time, when we have got these statements prepared and presented.

MR. FRAWLEY: They are just a lot of figures at the moment.

THE CHAIRMAN: I have not the same ability as my fellow Commissioner has, in understanding statements, and so I warn you both that at some time I expect you to put in simple language so that it may be understandable to anyone who does not perhaps happen to be a chartered accountant, the result of these statements.

MR. FRAWLEY: Well, I am quite sure that is what we are trying to do, and that is why Dr. Brown is here.

THE CHAIRMAN: I do not at all pose as a chartered accountant, and never have, but I am of the opinion that all figurations are but means of arriving at a result which can be stated in words.

MR. FRAWLEY: In words.

THE CHAIRMAN: Yes, and the method of approach to the conclusion arrived at can surely also be put in words.

Q MR. NOLAN: May I ask Mr. McGrath, the value of the fixed assets as contained in this Exhibit "311" is based upon what?

A That $5,289,268.42.

Q Yes?

A The cost of the equipment in the plant at the present time.

Q Is that book cost?

A Yes, that is what was spent for that equipment.

Q That is the actual cost shown by the books?

A That is right.

Q And you want to discuss that angle of it with the experts?

A Yes.

Q As to whether that kind of cost should be taken?

A That is right.

Q MR. FRAWLEY: Or the alternative, namely, the present day replacement value, or some such thing as that?

A Well, I do not know whether you wish to get into the question of appraisals, I do not know whether you want to go into a long investigation like that.

J. McGrath

Q Certainly I do not, for myself?

A So I thought in discussing it with Dr. Brown and Mr. Cottle we could come to something which is fair.

Q But it would mean, even if it was an agreed figure, it would amount to an appraised value of your plant.

MR. NOLAN: Well, an agreed value.

A An agreed value, I think.

Q Well, all right, whatever it is, but it has to be thoroughly discussed?

A Yes.

MR. FRAWLEY: So I cannot add anything to it, Mr. Chairman.

THE CHAIRMAN: No. Of course, your method of approach is vitally important, your method of approach in arriving at the value is vitally important if the value is to be vitally important, because your results would largely depend upon how you approached them.

MR. FRAWLEY: Yes.

THE CHAIRMAN: We had a little experience of that in the pipe-line matter.

MR. FRAWLEY: Yes, just a little. Well, have you any more figures?

A No, that is all, sir.

Q Now these statements then will, after they are discussed and re-discussed, will complete your evidence to the Commission, I take it?

A That is right.

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THE CHAIRMAN: I suppose, Mr. Frawley, you think it would be of no use to attempt to go on with anything more today?

MR. FRAWLEY: No, Mr. Chairman.

THE CHAIRMAN: Supposing Dr. Brown and Mr. Cottle and Mr. McGrath have not reached any conclusion that will advance us by tomorrow morning, have you anyone else to go on with?

MR. FRAWLEY: No, because it really stops things. Mr. Halverson, I wanted to follow with.

THE CHAIRMAN: What I was thinking about was the tag ends.

MR. FRAWLEY: Oh yes, yes, ther seems to be always some of those.

THE CHAIRMAN: If we could eliminate them.

MR. FRAWLEY: Yes, I have one or two producers.

THE CHAIRMAN: Unless you wish to finish with those who are concerned with the accounting end, it would occur to me if you have anyone else left, for example, on the cost of production.

MR. FRAWLEY: Yes.

THE CHAIRMAN: The field price or any tag ends which you have, that we could use odd days in cleaning them up.

MR. FRAWLEY: I think I will stay with my people this afternoon, and in the morning then we might go on, if they are still discussing it,

we might go on with Mr. Maynard Davies, and one or two like that.

THE CHAIRMAN: We will leave it with you, Mr. Frawley. We will then sit at 10:30 tomorrow morning. You have nothing more to put in this morning, Mr. McGrath?

WITNESS: No, sir.

(The Inquiry was here adjourned to be resumed at 10:30 a. m., June 14th)

J.J. Frawley

The Province of Alberta

IN THE MATTER OF THE PUBLIC INQUIRIES ACT

—and—

IN THE MATTER OF a Commission, dated the 12th day of October, A.D. 1938, to inquire into matters connected with Petroleum and Petroleum Products

Commissioners:

The Honourable MR. JUSTICE McGILLIVRAY (*Chairman*)

—and—

L. R. LIPSETT, ESQ.

Session:

CALGARY, Alberta JUNE 14th, 1939

VOLUME 77

Brown
8952, lowest cost refiner sets price

I N D E X

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E X H I B I T S

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(EXAMINATION OF MR. JAMES McGRATH CONTINUED BY MR. FRAWLEY).

THE CHAIRMAN: Mr. Frawley, I see in the morning paper a statement that this Commission adjourned to consider reports behind closed doors.

MR. FRAWLEY: I didn't read it this morning, I had so much else to do.

THE CHAIRMAN: Now this Commission has been very careful to make it clear that none of these proceedings are behind closed doors. We adjourned yesterday afternoon in order that experts might talk to each other in the afternoon instead of doing it far into the night. There was no sitting of the Commission whatsoever nor were the Commissioners together nor were they considering anything relating to this Commission and I want that quite clear.

MR. FRAWLEY: Yes.

THE CHAIRMAN: And I trust that whoever saw fit to make that report will see fit to say that it is not so.

Q MR. FRAWLEY: Mr. McGrath, I understand that you want to make some slight changes, do you?

A Yes.

Q To the Exhibits that you filed yesterday?

A Yes.

Q Yes, would you do so now, that is in the Exhibits of yesterday and you have that, starting with 300?

A Exhibit "310".

Q Exhibit "310" is what you want to change?

A Yes.

Q Yes?

A In 1938 the crude run was 2,753,587 and the cost----

Q That is a change from 2,855,527?

A To 2,753,587.

Q It is now 2,753,587?

A Yes.

Q THE CHAIRMAN: That is the 1938 figure?

A Yes, 2,753,587 and the cost per barrel in the last column opposite 1938 is 43.31 instead of 42.72; that also changes the average for the nine years at the bottom, the barrels run is 1,813,709 and the average cost in the right hand column is 63.94 instead of 63.54 and below that----

Q It does not touch your manufacturing costs at all?

A No, and below, the processed for Imperial instead of being 2,474,294 should be 1,972,354 and that gives the total for 1938 of 2,753,587; now a similar change on Exhibit "280", Schedule 3, manufacturing costs, the barrels charged at the top instead of being 2,855,528 should be 2,753,587 and the cost instead of being 42.72¢ per barrel should be 44.31.

THE CHAIRMAN: Mr. Frawley, Mr. Cutler has just asked about changing the original exhibit. There is no objection so long as the change is verified by the witness as it has been done and I am just wondering if you shoudl not do that because we might not be reaching a consideration of these statements for some weeks.

MR. FRAWLEY: No.

THE CHAIRMAN: And it might be just as well to have it in its proper form, less we overlook what Mr. McGrath has said by way of change this morning.

MR. FRAWLEY: Instead of picking up the Exhibit sometime without the change and using it in that way.

THE CHAIRMAN: Yes.

MR. FRAWLEY: Well I suppose Mr. McGrath is

the one to do that, the Exhibits are not being used and perhaps that could be done at the noon hour, that is make the actual changes?

A Yes, I would be very glad to do that.

Q MR. FRAWLEY: Mr. McGrath I want to ask you about this figure which you have just given us, of manufacturing costs, barrels of crude charged?

A Yes.

Q You have now given us a figure of 2,753,587?

A Yes.

Q Is that the figure after you have made adjustments for inventory?

A No sir, that is just taking out the naphthas and that which was sold without being processed; with the inventory adjustment it is still 45.61 as shown on Exhibit "308"(C).

Q What is that you say about "308" (C)?

A The manufacturing costs after considering the inventories of unfinished stock is 45.61.

Q Yes?

A That remains.

Q That remains the same?

A Yes.

Q Then this is a new figure you have given us of 2,753,587 as the actual number of barrels of crude charged to the stills?

A That is the barrels of crude charged, yes, that is based on the crude charged; now the unfinished stock inventory increased and applying the same number of dollars to the net amount of oil gives us this 45.61.

Q Is the 2,753,587 crude oil?

A No, that is crude oil and absorption.

Q Crude oil and absorption?

A All that is taken out are those things which are sold in the plant which we really do not pass through the process ing,- that is the naphthas.

Q DR. BROWN: Just in and out?

A Yes, Dr. Brown, that is based on the 69,032,397 gallons as shown on Exhibit "308" (C).

Q MR. FRAWLEY: You show a difference there, I think you should correct perhaps the exhibit "280" Schedule 3, with respect to the descriptive words "barrels of crude charged"?

A Yes, that is probably right, barrels of crude and other stocks charged.

Q Yes, barrels of crude and other stocks such as separator naphtha, absorption naphtha and so on?

A Yes.

Q Well that is another correction you might need to make on the exhibit?

A Yes, I will do that, Mr. Frawley.

Q Now is there anything else?

A Yes, you were asking me about the specifications of jobbers' crudes of gasoline.

Q Yes?

A For similar crudes the specifications are the same with the exception that on leaded gasolines we add solvent oil to our own crude.

Q To your own production?

A Yes, and of course the colour is different.

Q But other than that the Commission may take it that what the, say the North Star Oil Company sells as standard gasoline is identical with Three Star except it contains no solvent oil?

A If it is purchased from us, Mr. Frawley.

Q Yes, if it is purchased from you?

A That is right.

Q And that goes for all of the marketers who purchase petroleum products from your plant?

A That is right.

Q That they are product for product exactly the same except that your products, your own products contain solvent oil and theirs do not?

A Yes,and the colour varies.

Q Is that all?

A And you were asking me to file a statement on the B. A.'s processing agreement and I have it here.

Q Oh yes?

(Statement produced by witness).

Q This is a statement entitled "Processing Agreement, Income and Expense, exclusive of fuel as customers supplied the fuel", it does not say so, but this relates to your operation for B.A.?

A Yes.

(STATEMENT PRODUCED HERE MARKED AS EXHIBIT "312").

Q Now is that all, Mr. McGrath?

A That is all, Mr. Frawley.

MR. FRAWLEY: Thank you then. I will call Dr. Brown.

DR. GEORGE GRANGER BROWN, having been first duly sworn, examined by Mr. Frawley said:

Q Dr. Brown, your name is George Granger Brown?

A Yes.

Q And you live where?

A At Ann Arbor, Michigan.

Q And what is your occupation?

A I am professor of chemical engineering at the University of Michigan and consulting engineer.

Q Will you tell the Commission what your qualifications are, where you graduated and what your experience has been?

A I graduated with the Bachelor's Degree at New York University in 1917 and later received a Chemical Engineering Degree from the New York University and the Masters Degree and the Doctor's Degree from the University of Michigan; since 1920 I have been teaching at the University of Michigan and acting as consulting engineer, having charge of all the petroleum work at the University of Michigan since about 1925; I have been consulting engineer for many of the petroleum companies in the United States and the American Petroleum Institute, the Natural Gasoline Association, and also many of the engineering companies, Universal Oil Products and Kellogg's and so on.

Q Have you appeared before Commissions and Courts as a witness?

A Yes I have, both in the United States and Canada.

Q And in Canada you have been appearing where?

A At Ottawa.

Q At Ottawa. You appeared before the Tariff Board a year or so ago?

A Yes.

Q And that was with respect to a matter involving Turner Valley crude, was it?

A It was.

Q And an analysis of that crude as compared with Mid-Continent crude in the Imperial plant at Sarnia?

A That is right.

Q And in the United States you have been appearing I suppose in

[illegible]

various States, in many different States?

A I have appeared before many of the Federal Courts in various Districts as well as the State Courts.

Q Now you have been asked, Dr. Brown, you have been brought here by me to give to the Commission the benefit of your experience as a witness and also in a consulting capacity to myself and Mr. Cottle, is that right?

A That is correct.

Q And you have made some study of the opertations which the Imperial Oil has in Calgary?

A I have.

Q And you have seen their plant?

A I have.

Q And you have seen the costs statements which Mr. McGrath has brought with him from Toronto?

A I have.

Q Now it occurred to me, Dr. Brown, before you proceeded to discuss the Imperial Operation or any other operation in the Province, that you might give to the Commission an exposé of what is involved in petroleum refining, both elsewhere and here, and then go from that into a discussion of the particular operations which we have to deal with in this Province, and I do not know whether these charts would be of any help to you in explaining it but I would like you to give to the Commission an exposition of petroleum refining so that they will know what it is all about?

A The problem of the petroleum refiner is to take the crude oil as it is delivered to him from the pipeline and process it so as to produce those products which are desired in the territories served by the refinery. In many ways the operation of a refinery is analogous to that of a railway. The railway

takes the raw material or the products from one part of the country and then has to deliver the various products at various points along its right-of-way. The refinery takes the crude oil as it comes from the pipeline and processes the crude oil, delivering products from the crude oil stream as it flows through the refinery at various steps along the refining process; for example what we call "topping" is the first operation to which the crude is ordinarily subjected; the "topping" the crude oil flows through the furance or the shell still or other device to heat the crude oil to such temperature whereby vapouring, from the crude oil, produces gasoline and some of the distillates which would compose the kerosene and tractor distillates;that is in many ways equivalent to simply carrying the crude a short distance to the refining process as a railway may carry some of its freight only a short distance. After these materials are "topped" from the crude they then have to be treated to make them suitable for use in motor cars or in lamps as burning oil; that involves a little further operation. Sometimes it costs more with some crudes than with others and it is again comparable to the railway carrying its products a little further along the line.

Then the cracking operation is an expensive operation in which the unvapourized crude oil left behind from this "topping"operation and frequently along with some of the material which has been vapourized from the crude but which is not considered just suitable for marketing in that form, may be mixed with the heavy ends from the crude or processed separately; those materials are then heated to high temperatures and usually under relatively high pressures in equipment which is expensive and has to be carefully inspected

to prevent serious fire and again this is equivalent to the railway carrying some of its products perhaps over a high mountain, an expensive haul for the railway and an expensive operation for the refinery. Those products are then further treated, sometimes re-run, in order to make them suitable for the market. Now it is clear that the refining plant for the refinery must have a certain size of equipment or a certain capacity in its equipment in order to handle any appreciable amount of crude oil and in operating this equipment there is a certain minimum expense incurred, in other words there has to be a certain number of men on the shift, each of the 24 hours. Supposing we had one unit, we have three men on a shift. Now it does not make any difference whether we are processing 50 barrels or 5,000 barrels, it is going to require just about the same number of men to operate that plant for, that particular part of the plant for that particular shift in the same way as it takes the same train crew to operate a train whether it consists of one car or sixteen cars, so the cost of operating the refinery is by no means constant for the same amount of crude being processed. If the refinery is operating up to its capacity, that is equivalent to the railway operating the heaviest trains that the locomotive can pull, it means that all of the energy of the operating forces are used most efficiently; on the other hand if the amount of crude being processed is cut into half of the capacity of the plant, the number of men employed to operate the plant is substantially the same, the depreciation on the plant is the same, and the taxes would be the same; the only factors which would be decreased would be the proportionate, possibly a proportionate decrease in fuel and in the chemicals used.

The upkeep might be decreased slightly due to the lower capacity at which the plant is operated. Now for that reason any calculation as to the cost of the operation of a plant or any calculation or estimate as to the cost of producing gasoline and other products from crude oil must take into consideration the relative capacity at which the plant is operated. That has been brought out, I think, rather clearly by an Exhibit presented by Mr. McGrath to which I might call your attention. It is Exhibit "310" which shows the cost, as computed for the Calgary refinery of the Imperial Oil Company over the past eight years. That indicates in 1938 when some two and a quarter million barrels of crude were processed --

THE CHAIRMAN: Before you proceed, do you mind giving us the benefit of your views on a situation such as we have heard of where a refinery is operating part of the time and shut down part of the time? I quite appreciate what you have said and I agree that if they handle a greater volume, that the refinery is capable of turning out the product. But what have you to say as to the situation where the refinery operates in a busy season and closes its doors in the winter time, such as here for example? What would occur then?

A Suppose we operate for six months and shut down for six months. This is a hypothetical case.

Q Yes?

A It is necessary of course to maintain a skeleton crew. That is your superintendent and your chemist and your responsible foremen really must be kept on the pay roll

because these are trained and experienced men and it is impossible to pick these men up at a moment's notice. In fact it is considered rather poor practice to allow even any of the operating force to work intermittently like that because they are really all skilled men and about the only men you could drop from the pay roll without a very noticeable loss in efficiency would be what we might call the unskilled labor or the men about the yard. So that it means that the Company must maintain a skeleton organization, in much the same way as a railroad must maintain a skeleton organization. It has to maintain its right of way and have men available to start up when the occasion arises. Now there are two ways that a refinery can meet that proposition. One is just as you have mentioned, to run the refinery for the six months out of the year and then shut down for the other six months, in which case they would have to have a plant of perhaps fifty per cent greater capacity than if they could operate that plant - well maybe twice the capacity than if they could operate that plant up to capacity twelve months out of the year and then store the products during the winter and ship them out during the summer. I believe the Imperial Oil Company here has found it more satisfactory to operate on that basis. That is to operate the plant practically up to capacity twelve months out of the year. Not right up to the bottle neck but practically up to capacity twelve months out of the year and then purchase storage tanks so that during the winter months they are processing distillates and other things that cannot be marketed at that time but which will

be marketed the following summer. If they operate that way it means they must have more capital tied up in semi-finished products and more capital tied up in storage tanks. On the other hand they would then have a plant of smaller capacity being able to serve the same community. So it is a balance between purchasing more storage tanks and keeping more products in storage, or putting in a larger plant and maintaining a crew for operating that plant in an idle condition during maybe four to six months out of the year. As a general rule I think that it is found to be more economical, more efficient certainly and usually more economical to put in the additional storage and operate the plant as near capacity as practicable so that the crew is busy twelve months out of the year and then the products are put into storage during the winter months and shipped out of storage during the summer months. Any such problem of that kind demands its own individual study because it all depends on how the markets change. But in almost every case I have been in it has appeared more economical to operate in that way, rather than to put in a large plant and to run it for six months and then shut down. You will find, however, that a number of very small so-called skimming plants, which simply take the crude oil and skim off some gasoline and tractor distillates and are not equipped to process the residue, will operate in the way you have mentioned. For example, there might be a number in Turner Valley which will process perhaps 200 or 300 barrels a day during the season when there is a good demand and then as soon as there is no demand they will shut down. Those plants are marginal producers in the sense they are inefficient. Their

original cost is negligible. They are really nothing but junk. Sometimes they are very dangerous to operate in case they are not properly inspected. No community could depend upon such an operation to really meet its requirements. But you will find some of these, and these plants have such a small investment and such a small crew to operate them that they will find it more economical for their particular condition perhaps to operate at capacity only during the period that there is that demand for the product and then shut down during the winter. But in this case, particularly with the Imperial Oil Company, we are not facing that situation and they have found it more economical to operate the other way. Have I made that clear?

Q Yes.

A If I talk too long I wish you would stop me, because I have been told I should begin at the beginning and go right down.

Q That is precisely what we want. We are quite uninformed and we will be glad to have any education you can give us.

A If you interrupt me whenever you wish any information I know it will help me a good deal. // As I indicated on this Exhibit "310" it could be seen that the operating cost per barrel of crude put through the refinery has varied in this one refinery from a low of about 44 3/10 cents in 1938 to a high of about 84 cents in 1933. Roughly the quantity of material, crude processed in 1938 was something more than twice that in 1933. So there is the same refinery operating in much the same manner but the difference in through-put has practically doubled their

[illegible]

cost - rather the increase in through-put from 1933 to 1938 has practically halved their cost of processing one barrel of crude. Very much the same experience as, of course, in that of the railroads where they find when traffic decreases and they have to maintain their right of way and maintain their crew and maintain their equipment that they lose money with the same rates, while under other conditions, with much heavier traffic, they can make a very substantial profit. So that the actual cost of processing crude oil in a refinery to convert it into gasoline, distillates and other finished products depends in a very large measure upon the amount of crude processed through the refinery. In fact I believe that may be safely stated to be one of the most important variums. There are differences in efficiency and differences in other operating costs but that one factor makes more difference than practically all the rest put together. In the United States, with operations with which I am more familiar, we find operating costs of a plant of around 5000 or 6000 barrels through-put vary over quite wide limits and based on the experience I have under United States conditions, and making some allowance for increased costs in Canada due to increased costs of equipment and also it appears that with a refinery out here in Calgary far removed from other technical staffs, such as there might be in the East, they have to maintain adequate technical staffs here to answer all of their problems, it seems that the operating costs here at Calgary may vary apparently about oh, 5 to 10 cents per barrel than we might expect to find in the United States under similar conditions.

THE CHAIRMAN: Because of the technical staff?

A Well, let me elaborate on that a moment.

Q We can find out I think........What was the evidence, Mr. Frawley, with regard to some arrangement with.....

MR. FRAWLEY: The Standard Development Company.

THE CHAIRMAN: We have not a technical staff to any extent here, as I understand the evidence, Dr. Brown, but there is some arrangement made with a subsidiary of the Standard Oil.

MR. FRAWLEY: Called the Standard Development. This is listed as an item of manufacturing costs and there is shown under manufacturing costs an item of $27,805.07 described as engineering development. Mr. McGrath explained that that was a fee or charge made to get, as they do get, the benefit of the engineering advice and technical advice of a subsidiary of the Standard Oil of New Jersey known as the Standard Development Company.

THE CHAIRMAN: And they have the right to make use of patents.

MR. NOLAN: I wonder if Dr. Brown is talking about operating technicians?

A I did not have a chance really to elaborate on what I had in mind. I think I can clear that up in a moment.

Q MR. FRAWLEY: You know what we mean when we say the Standard Company?

A Yes. Take for example a plant built in the United States, a modern plant with 5,000 or 6,000 barrel capacity. It can be built down there for a certain cost. I have not had charge of any erection work in Canada, and I do not know the exact difference, but as near as I can estimate,

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the cost of constructing that same plant in Canada, a place such as Calgary, might be from 25% to 30%, or possibly, more, due to tariffs and other conditions. So that there is first of all the increased cost in the plant as erected in Canada as compared to the same plant erected in the States. That in turn would increase the cost of operation because the depreciation will be proportionately larger. That is one of the items. Another item which I rather passed over and apparently did not make very clear is that a refinery here at Calgary has to depend very largely upon its own personnel to keep the plant operating in an efficient manner, while a plant adjacent to a large industrial centre such as Chicago or Detroit, can frequently run into Detroit or Chicago and get repairs made by other shops independent of their own, and they can also get expert electrical service on their electrically controlled devices, and pumps and so on. So that a refinery at Calgary, in order to maintain an efficient operating condition, has on its staff and in its refinery proper shop facilities and expert technicians which could probably be discpensed with, at least to a certain degree, by most of the American or Unites States refineries which are in the large centres.

So, taking these factors into consideration, and making an estimate which I am giving simply for what it may be worth........I do not know whether it would stand up on very careful inspection..... but it appears that the operating cost for a refinery in Calgary would be, I believe, somewhere between 5¢ and 10¢ more per barrel. That is a refinery operated under

equivalent conditions and under equally efficient conditions. I am saying that simply because any comparison that is made in operating costs say in the Chicago district and the operating costs at Calgary, must take into account those differences. Exactly what that difference is, I am not prepared to state, but it appears to be something of that order.

Now, I have gone through the figures as presented by Mr. McGrath, with his co-operation, yesterday, and as set forth on Exhibit "~~380~~ 308" C I would like to call attention to the fact that these figures as given in Exhibit "308" C do not represent the actual operation of the Imperial Refinery for the year 1938. They really represent what would have been the results of their operation in 1938 if the prices had been constant throughout the year, and equal to what they were during the last six or seven months of the year 1938. I have been informed, I think, that the prices of the finished products from the refinery were reduced early in the summer of 1938, and that this analysis is based on the prices as they existed from about June through to December, 1938.

Now, the figures as given there correctly portray the costs and have been........

Q MR. FRAWLEY: Do I understand you, Dr. Brown, putting these reduced prices which came into effect on the 22nd of June back to the 1st of January, 1938?

A That is right. That is the actual realization or income during 1938 for the Imperial Oil Company was greater than the figures as shown here. Because these figures have been adjusted for that price change and the figures on "308" C

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represent what would have been received if the price had been constant throughout the year and equal to what it was subsequent to June.

Now, another point I wish to make. The figures given there correctly portray the cost as based on the operations as conducted in 1938, during which the Imperial was processing something like three-quarters of a million barrels of crude oil for the British American, and as I pointed out a little earlier the cost per barrel processed in the refinery fluctuates very widely with the amount of oil being processed. So that on the other hand, if the Imperial Oil Company was not processing this, roughly, three-quarters of a million barrels of crude oil and naphtha for British American during the year 1938, their costs would have been quite different from the figures given on Exhibit "308" C. I made an estimate in which I had pro-rata reduced the chemicals, the supplies, the fuels, the electric power, according to the amount of crude that would have been processed if the Imperial had been processing only the crude necessary to supply their own markets. I estimated the cost on that basis came out to be 59¢ per barrel instead of 45.06¢ per barrel. And if we compare that figure, which is an estimate of mine, of 59¢ per barrel for processing approximately 2,000,000 barrels of crude - the exact figure is 1,972,354 barrels - you will see that that compares fairly closely with the figures given by Mr. McGrath on Exhibit "310" for the year 1937.

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In the year 1937, the number of barrels run was slightly over 2,000,000, and the cost per barrel as given is about 61¢. So that condition as it existed in 1938 shows a cost of about 45¢, 45-61/100 cents per barrel. Suppose the operation during the year 1939 was exactly the same, except for the fact that the British American are processing all their own crude - that is a hypothetical condition which does not exist - but if that were the condition, you could say the cost on the same basis would increase approximately 13¢ or 14¢ per barrel.

Q MR. COMMISSIONER LIPSETT: In that connection, Dr. Brown, did you consider on the other hand what the effect would be of the Imperial themselves voluntarily reducing the throughput by about 1,700 barrels, which they transferred to the Sarnia refinery?

A 1,700 barrels?

Q 1,700 barrels a day, 1770, I think it was.

MR. FRAWLEY: 1,770.

A Any decrease in the throughput of the refinery will increase the cost per barrel put through the refinery. Do you mean you would like to have.......if I understand your question, an estimate as to what the cost would be if they were processing, say........

MR. NOLAN: Excuse me, is not the fact the evidence shows that the reduction in throughput was the throughput for the Regina refinery as being the distributing centre for that area?

MR. COMMISSIONER LIPSETT: And nothing to do with Calgary at all?

MR. NOLAN: I understand not, sir.

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MR. COMMISSIONER LIPSETT: Possibly that is right.

MR. FRAWLEY: That is right.

MR. COMMISSIONER LIPSETT: That does not arise then in connection with Calgary, Dr. Brown?

A I believe that is about all I need say to explain the cost of operation as shown on this Exhibit "308" C. In arriving at those figures, I might point out that I have checked all of the figures used with the records that Mr. McGrath brought with him. I am not going back to the original expense vouchers, but I mean I checked the analysis he has presented, and there are one or two minor, two minor items, which perhaps ought to be mentioned. One is that in this analysis as presented the loss in stabilizing the casing-head or the natural gasoline has been charged against the crude and naphtha processed, even when that loss was due to natural gasoline which was simply brought into the refinery, stabilized, and then sold. That makes a difference of about $10,000.00, which, in the over-all figure, would make a difference of not more than ½¢ a barrel. I think it is of no consequence but I should perhaps call attention to that so that the record will be clear.

So that the cost, then, as shown on Exhibit "308" C may be reduced by ½¢ per barrel, making it read 45.11¢ instead of 45.61¢, if this factor had been taken into consideration on a little different basis.

Then there is the item of depreciation. That is put in at, I believe, $283.473.70 as the depreciation to be written off during the year 1938. That seems to be a reasonable figure based on original cost

and the depreciations that have been indicated to depreciate that plant during the past fifteen years. However, no effort has been made to estimate whether or not the cost of the plant as it was originally installed would be considered an economic and efficient investment at this time or not. It simply shows the historical presentation of the depreciation which the Imperial Company has consistently allowed over the past fifteen years. If that depreciation figure were changed, that would of course, in turn, affect the cost of processing crude. If that figure should be changed $50,000.00 that would change the cost of processing crude by about 2⅛¢ per barrel.

Q MR. FRAWLEY: For each $50,000.00 of change?

A Approximately.

THE CHAIRMAN: For each $50,000.00 change in depreciation?

A If the depreciation, for example, were $233,000.00 instead of $283,000.00, that would mean a smaller depreciation by $50,000.00 a year. That would make a difference of approximately a decrease in cost of processing of about 2⅛¢ a barrel on the throughput of 1938. It would affect that differently with different throughputs. So that I feel that this figure given on Exhibit "308" C, represents a figure that might be taken at its face value, subject to any correction that might be made in the depreciation. But the depreciation in turn on the face of it appears consistent with the analysis presented by Mr. McGrath.

Q THE CHAIRMAN: Depreciating over how many years and at what rate?

A That is depreciating about fifteen years from the original cost of $5,289,268.00 as shown on Exhibit "311" down to the present value of $1,845,142.00.

(Go to Page 8929).

This depreciation of $283,000 for the year 1938 appears entirely consistent with the figures.

Q Now I think you might stop there and say what statement has been made to you by Mr. McGrath with respect to how the depreciation reserve of $3,444,126.25 has been built up to arrive at the depreciated figure of $1,845,142.17?

A Well I think he can probably speak for himself better than I can how it was done but my understanding is that figure was arrived at by taking the consistent depreciation during the 15 years, as compared with the depreciation taken during 1938; in other words the same principle of depreciation was applied during all of the 15 years between 1923 and 1938, that is simply a statement he made to me and it appears to be true.

Little real different

Q Yes, and what do you say about that assuming that the Commission will accept the original cost figure of 5 million odd, assuming that is sound and worthy of acceptance, then what do you say with respect to the manner in which Mr. McGrath has built up his depreciation reserve?

A Well I have not gone into that thoroughly. I simply have seen the result in the presentation and it appears sound and consistent to me.

Q All right?

A I believe that is about all I need to say regarding the cost of refining. I might point out----

Q THE CHAIRMAN: Well now, well go ahead.

A I say I may point out the relationship between the selling price of the gasoline at the refinery and what effect that would have on the return to the refinery. Under----

Q THE CHAIRMAN: Now before you enter upon that phase of your discussion Doctor. We have a figure which

must come into the cost of production of refining a barrel of gasoline, which is depreciation?

A That is right.

Q The amortizaition of the money invested, the capital money invested in the refinery?

A Yes.

Q Now that being so it is important I suppose to determine as to whether or not there was prudent investment in connection with the refinery?

A Well----

Q Supposing that we have a plant here that is put down at a capital cost of $2,000,000 more than it should be, would that not affect operating costs?

A Yes, but that will affect depreciation.

Q Yes, it is bound to affect the cost of refining a barrel of gasoline. Now you said, as I understood you, that you were not familiar with the cost of constructing a refinery of 5 or 6 thousand barrels a day in this country but you would figure it was 25 or 30 per cent more than it was in the United States?

A That is correct.

Q What is the cost in the United States, generally speaking?

A A modern plant----

Q Of that class, of course?

A Of 6,000 barrels, is that a fair capacity to take?

A Yes.

A A modern plant of 6,000 barrels capacity in the United States, not including storage nor land, would probably be built for somewhere around a million and three-quarters; now if we add storage to that which in the United States you might figure at around 70 cents a barrel, you might add another three-quarters

[illegible]

of a million dollars for storage, which would bring it up to about two and one-half million dollars; to that we would have to add land and there would be some other auxiliaries which I should imagine, the full cost I should imagine would be somewhere about two and a half or three million dollars for a plant that would produce primarily motor fuels and burning oils and fuels of that kind; not lubricating oils or asphalt.

Q We have no opinion at present of course as to how this approach should be made to any recommendation that we have to make but do I understand that, having regard to the plant you have seen here and the storage you have seen here and taking everything into account that in your view would be necessary, that an economical substitute plant would be erected today for two and a half to three million dollars?

A Not here.

Q No, you would add 25% or 30%?

A Yes, I would think I would be inclined to add about 30% to that and I can imagine that it would be possible to build a plant, of course this is nothing but a curb stone opinion you understand, I have previously disqualified myself for any exact information as to costs here in Canada but I should imagine that from 4 to 4½ million dollars would probably build a plant of 6,000 barrel capacity of modern construction at this time, that would handle 6,000 barrels per day and also contain probably sufficient storage to operate throughout the year.

Q How much are you allocating to storage, Doctor, in that?

A I should say roughly a million dollars, that is roughly, yes, roughly a million dollars.

Q MAJOR LIPSETT: In that depreciation item of

$283,473, odd, if that was on a straight basis over the 15 years it would be considerably more than the sum that has been taken off up-to-date?

A Yes.

Q Did you look into that at all?

A Let me put it the other way around, perhaps, we take the $3,444,126.25 depreciation over the 15 years and divide that by 15.

Q Yes?

A We then come out with about $230,000, instead of $280,000; now that again is not a sound way to depreciate a plant because the office buildings, the loading racks, tankage and a great deal of the equipment is good for, well, from 20 to 30 years and should be depreciated at perhaps around 3 or 4 percent; on the other hand the cracking plant , and a lot of the chemical treating equipment will depreciate much more rapidly than that and should perhaps be written off entirely inside of six or eight years and that difference between the straight line over-all depreciation, which would correspond to $230,000 and this $283,000, would have to be considered in the view of new construction which might have gone in during the past 15 years and which may depreciate pretty rapidly during the last two or three years and study the thing from the standpoint of each individual piece of equipment in the plant, that is why I say that the depreciation over-all looks consistent but if it was to be taken as a straight line depreciation on the assumption that all of the 5,000,000 dollars was invested in 1923 and that all of it had depreciated at the same rate,-which of course is not a sound assumption,-we would still have $230,000 depreciation in 1938 which in turn would have decreased the cost of processing crude by about 2½ cents per barrel.

Q MR. FRAWLEY: That, you think, is all that you have in mind to say about depreciation?

A Well depreciation is a subject that a man can elaborate on for hours on end but I do not believe with the information before us we can do much more than that.

Q THE CHAIRMAN: Well we had better have this witness' views, if he has any, upon how one should depreciate, at least what one should do about arriving at the present capital value ?

MR. FRAWLEY: Yes.

THE CHAIRMAN: You see we have, before we have run into the question of whether or not original cost associated with the prudent investment theory or without it, or the observed method of values plus observed depreciation should be adopted, have you any views about that, we are talking depreciation at this minute, and this Commission has had a little experience of having a difference of opinion presented as to how depreciation should be arrived at.

Q MR. FRAWLEY: Yes, and what has gone before, Dr. Brown, you understand the Commission has completed its work with respect to the pipeline rate and has in fact recommended a considerable reduction in the then existing pipeline rate, and the matter of the proper approach to ascertaining the amount of capital invested in the pipeline was a matter which gave us great concern and whether or not, there were two views offered to the Commission , whether or not the original cost should be taken less a proper depreciation or the present day replacement value less only observed depreciation, those were the two statements made to the Commission. Now the Chairman suggests to you that we are probably faced with the same situation precisely.

THE CHAIRMAN: But it may be an entirely different problem.

MR. FRAWLEY: It may be a different problem entirely. And I wonder if it would help----

THE CHAIRMAN: I was wondering what this witness thinks about that.

MR. FRAWLEY: I was going to say, I wonder if it would help if we had Mr. McGrath back for a few minutes to explain how the depreciation was arrived at. Perhaps that is not necessary. It has been discussed with Mr. McGrath and you know what he says as to how he arrived at his depreciation. Now for the record, we should have that made clear by Mr. McGrath and then you could resume your discussions of the subject, what do you think about that or do I understand you to say that you can discuss it with the Commission, as to what Mr. McGrath has done.

A Well so long as Mr. McGrath is here, he is able to speak for himself and I think it is one of the points that he can state exactly what was done, because my evidence is entirely secondary.

MR. FRAWLEY: That is quite right and if you will stand down Mr. McGrath will tell us how that was arrived at.

JAMES MCGRATH, having been recalled, examined by Mr. Frawley, said:

Q Mr. McGrath, will you take Exhibit "311"?

A Yes.

Q First let us see, without being critical at all, let me ask you, you have not, as I understand, the supporting data with

[illegible]

you to show, demonstrate how either the $5,289,268.42 was made up or the reserve for depreciation of $3,444,126.25 was made up?

A I have the details of the $5,289,268.42.

Q You have the details of that?

A Yes.

Q Let us just stop there and consider whether that should be put in, that is just what it purports to be, the addition of all of the capital investment which you have made from time to time at what the cost was?

A No, it is the cost of the plant which is in existence today, there have been items added and items taken out during that period but it is the cost of the equipment which is in the plant today.

Q Well that is something. If you built a still there or another piece of equipment in 1933 and it has gone out, it is not there at all now?

A No, that is right.

Q No part of that item is in this figure of $5,289,268.42?

A That is right.

Q So it is only the used and useful assets which you have included in your figure?

A That is right.

Q And as I understand Mr. Cottle has been supplied with the figures which build up to $5,289,268.42?

A That is correct.

MR. FRAWLEY: I think we might now put those in.

THE CHAIRMAN: Mr. Cottle may have been but we may not accept Mr. Cottle's view.

MR. FRAWLEY: No.

THE CHAIRMAN: If we have some figures behind this.

MR. FRAWLEY: Yes, the actual data.

Q MR. FRAWLEY: Will you look at these sheets and tells me if these are the sheets which show the resulting figure of $5,289,268.42?

A Yes, that is right.

Q Will you just describe them for the record?

A Well it shows the cost of the assets under various groups; for instance the crude stills, and the steam stills, and the cracking coils.

Q It is a classification of the company's assets?

A Yes.

Q Of the presently used and useful assets?

A Yes.

Q And they build up on the last page to $5,289,268.42?

A That is correct.

Q MR. FRAWLEY: Then the Exhibit consists of 6 sheets showing the cost of the fixed assets, used and useful.

(STATEMENT PRODUCED BY WITNESS HERE MARKED AS EXHIBIT "313")

Q MR. FRAWLEY: Now I do not suppose there are any copies, are there any copies of that handy so that you can send for them?

A No, these came from the accounting office in Sarnia.

Q But I mean there are some?

A Yes.

Q Without the reporters copying them all out?

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A I will have some copies made for you if you like.

Q That is fine. Now so much for the $5,289,268.42, unless you have something further to add about that, you have told us that they, that there is not included in there any asset which was in use at one time but which is not now in use?

A That is correct.

Q Well now, all right. The reserve for depreciation you have shown as $3,444,126.25?

A Yes.

Q And how is that made up?

A That was made up by the accounting department at Sarnia and on Exhibit "313" it shows the age, or the year in which the equipment was put in.

Q Each piece of equipment?

A That is right.

Q Each class?

A Each class of equipment, yes, that is right; for instance there was some put in in 1924, some in 1929, some in 1934 and so on.

Q Yes?

A Well by taking the rates of depreciation used in 1938 and applying them to the assets which were in use we determined the $3,444,126.25.

Q Now what do you mean when you say "using the rate of depreciation used in 1938"?

A Well over a number of years the depreciation has varied, say over the 15 year period, and we brought it to the 1938 period which is the basis used in our manufacturing costs.

Q Will you illustrate, in 1938, there was a certain rate of

depreciation on a certain class of equipment?

A Yes.

Q Can you give us the range of rates over the different classifications?

A Well I have not got them here with me, Mr. Frawley.

Q Just for instance, and I think your evidence should be supplemented by something of that kind, but for the moment there would be a rate of 7% on a certain class of equipment?

A Yes, and 5%.

Q 5% on another class of equipment?

A Yes.

Q Ranging between----

A Oh $1\frac{3}{4}$ to 7%.

Q From $1\frac{3}{4}$ to 7%?

A Yes, I think the average is about 5.3 or something.

Q Yes, now are those rates of depreciation which your company arrived at in their own good judgment or are those rates allocated to you or prescribed for you by the Income Tax Department?

A No, those are our own rates; they are lower than the Income Tax rates.

Q Now I wonder if that fully explains how that reserve was build up, the 3,000,000, it gives you now the depreciated value for your plant of $1,845,142.17?

A That is correct.

Q It is understood of course, I have always understood that you are going to send to Toronto and bring this supporting data?

A To Sarnia.

Q And bring all this supporting data?

A Yes, I will get the supporting data on that.

Q Oh yes, that is understood.

A I am sorry, it is a long distance off, that I am not able to have that with me now but I will get it for you as quickly as I can.

Q Yes?

Q MAJOR LIPSETT: Mr. McCarth, was there an actual figure written off each year for depreciation during the past 15 years?

A Yes there was.

Q And that is not the figure?

A No sir.

Q Well now can you give us the actual figure which was written off each year in your books over that period?

A I can get that for you, sir, yes.

Q I would be glad if you would get the actual figure?

A I will be very glad to get that. Of course it is of varying rates and they are not consistent, they are not consistent with the depreciation written off in 1938?

Q No?

A The reserves, and the depreciation written off against manufacturing in 1938 are consistent.

Q But if we take the book figures to get the corresponding net figure, you would require the book depreciation, would you not?

A Yes, and then we would have to change our manufacturing costs to conform to that.

Q Yes, and I would be very glad if you would get us the exact figure written off in the books for depreciation during the 15 years?

A Yes, I will gry to get that.

MR. NOLAN: Of course there would have to be a change in the manufacturing costs as shown by us in each year?

A That is right.

Q If the figure for depreciation is taken from the books.

MAJOR LIPSETT: Yes, but the actual fixed assets and the reserve for depreciation, that is really a capital item as distinct from operating costs.

A No, but that has a bearing on operating costs?

Q Yes I understand?

A For instance if the depreciation, this is based on 5.3; supposing it was 7% over the past 15 years or say 14 years, then the operating costs would have to be increased to that extent.

Q In the previous years?

A And in 1938.

Q Yes.

Q THE CHAIRMAN: Not once it was fully amortized, not once you got your capital back?

A That is right.

Q MR. FRAWLEY: I do not know what you mean precisely when you say would effect your manufacturing costs, whatever you established in the books for depreciation?

A For 1938, Mr. Frawley, we have used a rate of 5.3 for 1938 in the manufacturing costs and in setting up this reserve. Now let us assume for the moment the depreciation was 7% over the last 15 or 13 years, well then, if you are going to use that as the basis of valuing the plant, then the depreciation written off to manufacturing should be on the basis of 7%, it should be higher.

Q In 1938?

A In 1938, that is correct.

Q Of course what probably is in Commissioner Lipsett's mind is if the books show that the plant has been completely written off and some of the property was completely written off as early as 1935 or 1936----

A Well I can assure you that the plant at the end of 1938 was not written off.

Q By the Books?

A Yes, that is right.

Q As to any group of assets?

A Well I do not know about group but the plant as a whole was not written off.

Q That may be true but with respect to any group of assets they may have been written off, I am trying to understand the thing and you say it was not, that no part of the plant had been completely written off before 1938?

A I cannot say, that, Mr. Frawley, but I can say the entire plant was not written off.

Q But there might have been a smaller figure on the assets, of assets unamortized then, you say?

A That is possible, yes, that is possible.

Q And then what you would say about that is, well what would be your view about that, that the Commission should have regard to what you did in your books?

A Well I think this 1938 figure is the proper way to look at it; in other words the reserve is consistent with the amount of depreciation taken in manufacturing costs in 1938; I think they are related; if you use a higher, a lower valuation of plant then you use higher manufacturing costs so one off-sets

the other. I would like to have Mr. Cottle or somebody express themselves on that.

Q Yes. I think you are right about that and the only regrettable thing that Mr. Cottle keeps pointing out to me is that he is entirely at a loss to bring his mind to bear on the figures when he is only shown two figures there?

A I am telling you I will get that figure for you.

Q It might come by air mail?

A There is quite a bit of detail, Mr. Frawley, and it is a matter of getting it assembled.

Q I just wanted to point that out as indicating the reason why Mr. Cottle cannot make any very intelligent observations about it. I take it in the main he is in accord with that principle which you have just annunciated of consistency?

A Yes, I think he is.

Q MAJOR LIPSETT: It will be easier to understand it when we have the exact figures, whatever they are?

A Yes.

MR. FRAWLEY: Then I think for the moment that is all, Mr. McGrath.

THE CHAIRMAN: I want to ask something from Mr. McGrath; probably it is not for Mr. McGrath, no, I think that is all, Mr. McGrath. Mr. Frawley, just before Dr. Brown goes back into the box may I ask if you are exploring the position with regard to other refineries.

MR. FRAWLEY: That has been receiving a considerable amount of consideration, Mr. Chairman, and I am presently conversing with Mr. Harvey with respect to the B. A. plant. I think undoubtedly I will have to take the position that we must know all that we can know about the British American plant, the amount of capital invested, what there is there to represent the capital invested and as much as we can know about their present operating costs. I desire to say that publicly so that Mr. Harvey will know and I think he already knows that is my view. There would appear to be new considerations arising right along why we should know about that. For instance we have heard Dr. Brown say that a plant, he thinks can be erected to take care of a 6,000 barrel capacity for 4 to 4½ million in Canada. Well it would be very interesting and I think of great assistance to the Commission to know what the B. A. Plant has by way of capacity and what it has cost them to do that, and also, what is of equal importance, to have Dr. Brown's views on that operation.

THE CHAIRMAN: That is including the land and the storage.

MR. FRAWLEY: That is, the 4 to 4½ million is

including land and storage and to know what the British American has now of land and storage and what amount of capital has gone into that and what they have for their capital, what the plant is, what is had and what it can do. It has become very obvious I think that we must know pretty much all about the British American Plant.

THE CHAIRMAN: Or any other plant.

MR. FRAWLEY: That is so.

THE CHAIRMAN: Unless the Imperial can be selected as typical.

MR. FRAWLEY: That is right, that is right, well then we have two more plants.

THE CHAIRMAN: We are asked to say what is the fair price for gasoline to the consumer, as I recall.

MR. FRAWLEY: Yes.

THE CHAIRMAN: And we cannot do that without knowing what is,-not what may be fair for the Imperial to produce gasoline,they might produce it for very much less than some other plant or they might produce it for very much more.

MR. FRAWLEY: Yes I understand.

THE CHAIRMAN: But unless you can say that the Imperial is typical of all refinery operations that are efficiently and properly conducted----

MR. FRAWLEY: Yes.

THE CHAIRMAN: It must be supplemented by other evidence.

MR. FRAWLEY: Quite so.

THE CHAIRMAN: For the sake of discussing this point, supposing the British American can produce gasoline for a cost of 5 cents less per barrel----

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MR. FRAWLEY: That is important to this Commission in arriving at an answer as to what the fair and equitable refinery cost would be and then what the fair and equitable refinery price would be; then similarly we must have to explore the Gas and Oil Products Plant in Turner Valley, which is the next, I think, in volume per day, because there is a new cracking plant, and then there is the skimming operation of Mr. Plotkins, and that is being added to by a cracking plant during this coming season.

THE CHAIRMAN: Then I suppose some witness will deal with the whole subject as to whether or not public utility principles should apply.

MR. FRAWLEY: Yes.

THE CHAIRMAN: Or whether they should not.

MR. FRAWLEY: Yes, for my part----

THE CHAIRMAN: I am mentioning these things now that not only you but all other counsel may have in mind what is troubling us and we do not express the slightest opinion, for example, as to whether public utility principles should apply or not. We are not price fixing. We are merely asked to answer as to what are fair figures.

MR. FRAWLEY: Quite so.

THE CHAIRMAN: And that is all we shall do but we want to know how to approach it either through Dr. Brown or somebody else.

MR. FRAWLEY: Yes.

THE CHAIRMAN: Anybody who can assist us to that end.

MR. FRAWLEY: Yes, and I have brought to the Commission two men from the United States that are regarded as very eminent men, Dr. Brown, from Ann Arbor, Michigan and Dr. Fry, from the Department of the Interior at Washington and

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I hope that Mr. Nolan will also, if he thinks that the Commission will be assisted, will bring other eminent men here to tell the Commission just what you have outlined and how to approach the business of finding out what the fair and equitable cost of refining should be.

THE CHAIRMAN: And if Mr. Brown or anyone else can, we of course desire that he go behind the refinery door too. There are questions wholly unsolved so far as we are concerned yet in connection with the production of crude oil and field prices and so on, which have a bearing on the refined products.

MR. FRAWLEY: Yes I am not unmindful of that.

THE CHAIRMAN: I am generalizing now because it seems to me we must pretty soon get down to these really basic and troublesome factors which will have to be taken into account before we have to reach a conclusion.

MR. FRAWLEY: Dr. Brown is here also, as it is understood, to discuss the value of the Turner Valley crude at Regina, which enters into the question of the field price. That is quite a separate job and will be done quite differently.

THE CHAIRMAN: Quite so. Perhaps I should not have interrupted you, Mr. Frawley.

MR. FRAWLEY: All right, Dr. Brown.

DR. G. G. BROWN, recalled:-

Q BY MR. FRAWLEY: Dr. Brown, we interrupted your evidence to have Mr. McGrath tell us about depreciation. In the light of what Mr. McGrath has said, do you care to make any further statements, either particular or of a general nature, with regard to this question of depreciation in a refinery?

A Well the Commission has asked a rather pertinent question regarding depreciation, and whether or not the public utility principle should apply. I do not know whether your question is broad enough to open up that field for discussion or not.

Q THE CHAIRMAN: Well if not, consider it enlarged.

A I had regarded this investigation up to the present at least as being primarily historical. That is we were to find out what the situation has been and what it is. Now, if we are going to discuss the possibility of looking at it as a public utility, it seems to me, and I am speaking as an engineer and one with some experience in appraisal work, that we have either got to regard the refining of petroleum as a competitive industry in which there is competition, or else that the refining of petroleum has become a public utility such as the telephone industry. If it is a public utility it would appear that the way to handle it would be to grant a franchise to a company for the refining of petroleum, and then that one company would refine all the petroleum and supply all of the products needed for this territory, and that the consumers could then come to the refinery and buy what they wanted.

In other words, it seems to me you have got to go the whole hog and make it a public utility or else regard it as a competitive industry. I might also point out that your cost of refining will be quite different, perhaps, under those different methods of operating.

Q THE CHAIRMAN: For example, if it were a public utility no one would be concerned, at least this Commission would not be concerned with what the original cost of an obsolete plant was?

A That is right.

Q Whether right or wrong about that, you think that is right. That as a public utility, if it were a public utility you would not be concerned with the original cost of a plant that may have become obsolescent. I say not concerned, you would not be governed by it.

A If you were buying a plant and making it a public utility.

Q Yes?

A In the States at least they say that must be considered. I would say that perhaps it is not the controlling factor but it is one of the factors which I believe the Courts down there have held must be considered.

Q I would like to be clear. It is not for us to decide about whether it should be a public utility or whether it should not be. But something quite different. We are asked to say what is the fair price of gasoline, amongst other things, and that involves the cost of manufacturing, the cost of marketing and so on. All the questions we will have to deal with. The cost of manufacturing involves the question of what should be depreciated on capital investment. Quite aside from

Dr. G. G. Brown.

whether it is to be declared a public utility or not, surely you can give an answer of what is a fair price for gasoline under all the circumstances we are concerned with, whether or not we should look at the capital cost or look at something quite different, namely, the value of an economical and efficient plant set up today. Perhaps we should not do that. But if we are going to give a price that we say is fair, to be fair to the refiner and the marketer, and all these other bodies of people with whom we have to be concerned, then unless all the refineries are functioning at the same rate, the same depreciation costs, how would you arrive at it, if you took the original cost?

A Let us take the case as it exists, as it faces us right here in regard to the Imperial Refinery.

Q Yes?

A Let us assume that there has been expended in this plant something over $5,000,000.00 in capital assets and that those assets are now in use.

Q Yes?

A Then it would appear that the actual cost of processing one barrel of crude under the conditions as they existed during the latter part of 1938 was 45½ cents per barrel.

Q Yes. Now then, taking those same conditions and supposing the refineries which Mr. Frawley has mentioned, any one of them, cost say $2,000,000.00, your figure is immediately affected is it not?

A I was going to go one step further and assume another refinery, unnamed.

Q Yes?

A Just a hypothetical one.

Dr. G. G. Brown.

Q Yes?

A Puts in a plant, a modern plant and they find that they can process five or six thousand barrels a day at a cost of say 30 cents instead of 45 cents.

Q Yes?

A In order, however, to reach that cost of 30 cents a barrel they must process and sell 5000 barrels per day.

Q Yes?

A And they have got to get up to that throughput before they reach that cost. If they put only 2500 barrels through their cost may be 35 cents instead of the Imperial's 45.

Q Yes?

A The question then is what some other refinery would be able to process crude for and depends again very largely upon how much crude he is going to be able to process and sell.

Q Yes?

A If he can undersell the Imperial operation and you are in a state of competition, it would almost inevitably follow that the Imperial, in turn, would cut their refined price to meet it, with the result that both these refiners would then be making less money.

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Q At a greater operating cost?

A At a greater operating cost.

Q Yes. There are just some of the difficulties?

A That is right.

Q When you come to say what is a fair price today, or at the date discussed, to the public in respect of a gallon of gasoline?

A That is right.

Q How would you approach it?

A Well......

Q There are all these factors. It is simple to say "Well the Imperial costs are so much", and "Somebody else's costs are so much", with all the variables that if somebody else is going to take oil away from them then their cost will be more?

A Yes, and theoretically they should then raise the price of gasoline?

Q Yes.

A The fair price then would be higher than it would be otherwise.

Q And if that somebody else who takes it away has got a less capital investment involved he could do it for less even though he has less volume?

A That is possible. As I stated before it seems to me that we have to recognize that the industry is either competitive or it is not.

Q Yes?

A If it is competitive then we have to look at the cost of processing crude from the standpoint of competition, the way we have been just discussing it the last few moments. On the other hand if you want to look at it as a public utility, then we have to look at it as a public utility and our analysis is on an entirely different basis.

Q Well, Dr. Brown, just to put a supposititious case to you, supposing you had to give an opinion in your professional capacity......

A As to how it should be regarded?

Q No, as to what would be a fair price to the public

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[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

per gallon for gasoline, how would you approach it?

A I would start to analyze the situation on the basis that I found it. As I find it here, it is a competitive industry with, well, three or four refineries, producing the products desired from the crude oil. Then the lowest cost refiner would be the one which should set the price in a competitive industry. It would seem to me that the best way to do it would be then to analyze the operations of all of the refiners who are marketing in the territory and figure out what is the low cost for the refining of crude oil. In other words, what is the cost to the lowest cost refiner. And that should then set the price on the principle of free competition.

Q And if you were concerned with that in a local situation, would you be concerned to ascertain what the lowest cost refiner was doing in that locality?

A That is correct.

Q MR. FRAWLEY: How about volume?

A That is one of the factors.

Q Yes?

A The assumption would be in free competition......

Q Would you take the Plotkins', the Lion Refinery. That is the smallest of the four we have been talking about. The Imperial, the B.A., the Mayland and the Lion. I am just bothered about that. You could not take a plant that was too small, a four hundred or a five hundred barrel a day plant, could you?

A The small plant will not be the low cost plant.

Q No, he would not be this man which is the lowest cost refiner?

A No.

Q He might be.

THE CHAIRMAN: He could not be on the Doctor's theory as I understand it, because the one with the great volume will be lowering its cost.

Q MR. FRAWLEY: We first find which of the four is the lowest cost refiner, is that what I understand you to say?

A Yes.

Q Suppose we found Mr. Plotkins with just his 400 or 500 barrel a day plant was the lowest?

A Make that supposition.

Q That would not still advance your problem or that would not help?

A Let us make the supposition that Plotkins had a refinery - which I think is still a supposition and contrary to fact - and if he was able to produce the products required from that, and that he was the low cost producer.

Q Yes?

A Then he would set the price for the gasoline and the other products in this territory, because he could make a profit and sell it at these prices, which is a fair price. Then if the other people could not meet that price and still stay in business, he will enlarge his plant and he will continue to process the crude at no increase in cost, and still be able to make a profit and supply the entire market. That is the theory or the way an engineer looks at it. At least that is the principle of free competition.

[illegible]

Q THE CHAIRMAN: That presupposes, I suppose, Doctor, not only free competition but actual competition?

A That is right.

Q People may be free to compete and yet not compete?

A Yes.

Q And if an engineer were asked to give an opinion as to what a fair price would be would he go behind the actual situation of the price that was being charged?

A Right.

Q Even if it was being charged by three?

A Yes.

Q You would have to go back and find the cost and estimate what the fair return would be to that low cost producer, and that would be the fair price. Now he might be getting an exorbitant price and he might be glad to follow somebody who was getting an exorbitant price, and not change that in the least even though he could.

A Yes, he might be under a broad umbrella there, and making a big profit.

Q There must be exploration behind that to answer the question?

A Yes. You have to go back to the cost.

Q MR. NOLAN: I wonder if I might ask the Doctor a question?

THE CHAIRMAN: Certainly.

Q MR. NOLAN: Dr. Brown, can you compare the cost of a plant known as a skimming plant and another plant that conducts the whole refinery process?

A You could make a comparison between the cost, but they are

doing different jobs. They are doing different things, so that a comparison really is of no utility. In other words, I think when I answered this question put to me by Mr.Frawley, that if Plotkins had a refinery and if he were able to supply the products desired by this community from the crude, then such and such would be true. I do not believe that situation exists.

Q I was a little fearful that the Commission might have the idea that you could take what we have got here in this Province, four or five plants that there are, and take the lowest cost that exists in those actual plants?

A For producing all of the products required by this territory.

Q But when they do not produce all the products, does not that create a difficulty?

MR. FRAWLEY: Then we eliminate them.

A They are eliminated. They cannot do the job.

Q Nobody pretends Mr. Plotkins can produce anything but third structure gasoline at the moment. As I understand you that does not, with the rest, answer the Chairman's question.

THE CHAIRMAN: Why should not Dr. Brown's theory apply to third structure gasoline, if he is not making anything else? If he is not supplying anything else?

Q MR. FRAWLEY: What do you say about that? We will assume he is making third structure gasoline in reasonably large quantities. How about that? Does he fit in in any way?

A Let us suppose Plotkins' one plant which is capable of

making only third grade gasoline.

Q Yes.

A And nothing else?

Q Yes, that is the fact?

A He is unable to supply this territory with its requirements.

Q Yes, that is right?

A He might, because of conditions of free and open competition sell his third grade gasoline at a low price, which, in turn, will cause the other producers to reduce their price for that same product to equal his. Then he is faced with the difficulty of getting rid of the residue from his skimming or topping plant. This territory has a limited requirement for that residue, and unless one of the other plants is kind-hearted enough to take that residue off his hands, he will soon fill his tanks full of this residue and then go out of the picture. Then the people who can supply the products required by the industry will again be in competition with each other and that particular price of third structure gasoline will again rise. That has been repeated time after time over all parts of the United States. It is a matter of history. In other words, I have seen that same operation in my State in the past five or six years repeated many times. It is a marginal producer of a particular product who can exist only so long as the other companies hold an umbrella over him, and give him the protection that he needs to market his products. As soon as he stands on his own two feet, unless he is able to supply all the products required by the

[illegible]

territory he is serving, he goes out of the picture.

Q Because, one way or the other, out completely or into complete operation?

A Unless the other refineries hold an umbrella over his own operations.

Q Then he could continue with this one part of the market?

A Yes, as long as they are kind-hearted enough to take the other products away from him, or hold an umbrella over that operation.

Q He either goes out or he goes into the cracking operation and endeavours to supply all the products?

THE CHAIRMAN: Unless as the witness says he can get those taken away from him.

A But he is purely a marginal producer which cannot supply the products, the requirements of the territory.

Q MR. FRAWLEY: When he is only making one thing?

A Yes.

Q We are back then to finding the lowest cost refiner in the territory, and examining his operation, and he must be a person - well let us talk plainly about the British American Oil Company. They have certainly, as far as the market is concerned, considerably less of the market than the Imperial, so presumably their daily throughout would be somewhat less, although their capacity may be up to the capacity of the Imperial Oil. Do you think it is of value for us to endeavour to find the cost of the British American Oil Company, to find the refinery cost? You know something about the plant only having been built and so on?

A It is not yet really on stream.

Q What do you say about that?

A Well if the proposition were put up to me to determine what is the equitable price for gasoline and the other products as produced from the refinery in this territory at this time, I should proceed to get the information as to the cost of production from all of the refineries who are supplying these materials at this time, and set up a fair return on their investment, their operations, and say that that is a fair price as it should be determined by competition, as determined by the low cost producer.

Q Of course, let us be practical now.. Dealing with what we have at the moment. We have four, I think we can continue to talk about, the Lion Refining or Mr. Plotkins, and is not able to supply the market?

A That in my estimation would not be considered.

Q Mr. Mayland of the Gas & Oil Products Limited in Turner Valley is not able to supply the market. We know as a fact he is purchasing his first and second structure requirements through another refinery?

A He would be of no use in this consideration.

Q We have been told he is now actually constructing a cracking unit. You say he is not in the picture?

A If he is not in a position to supply all the products required he cannot be a determining factor in this price.

Q That eliminates the Lion and the Mayland. Then we have two left.

THE CHAIRMAN: You say he is constructing a cracking plant?

Dr. G. G. Brown.

MR. FRAWLEY: Yes. I put it to the witness he is constructing - when I say he is constructing a cracking unit, do you understand that to mean....

THE CHAIRMAN: Does that bring him into the picture.

Q MR. FRAWLEY: Does that bring him in or is it the intention at least to bring him into the cpmplete picture?

A As soon as he is in a position of supplying the requirements of the community as to the various products so that you could get the cost figure on his operations, then of course he should be considered.

Q Even though at the moment he has only a small part of the total gallonage, that would not throw him out?

A No.

Q As soon as he is in the picture and ready to supply all kinds of products from Ethyl to the lowest motor fuel?

A Well, even when he cannot supply all, but when he is supplying a substantial number of those products which are required - he may not be making any asphalt or something like that - but just the same if he is supplying only one product like third grade gasoline from a skimming plant, I know from experience that is not a real factor in determining what is a fair price for gasoline.

Q I want the benefit of your view, of what further exploration we have to make. At the moment we can eliminate those two plants. We do not know, and I have no knowledge as to when - I am told some time in August the Mayland Plant cracking unit may be in

operation.

A I do not know. Maybe that should receive some consideration. I do not know from what you say how capable that plant will be to supply the products.

THE CHAIRMAN: I am not at all sure that it can be eliminated so long as it can come in, even though it is not now in operation. Because ultimately, to provide us with an estimate of value it would appear to me at the moment that Dr. Brown has got to consider all of these operations and their effect if these other plants come in on the throughput that the particular refineries left will have. Take the Imperial for example. If it is established by competent evidence that there will be a plant put through by the Mayland interests in August in full operation, and it will in any sense reduce the throughput of the Imperial, then surely the Imperial is going to have a higher refining cost because of that.

Q MR. FRAWLEY: Let me put it concretely to you, if I may. The Mayland interests now sell a certain amount of first and second structure gasoline which they buy from the Imperial Refinery. Now let us take that out. Let us push that back on the Imperial Refinery and substitute some gallonage that Mr. Mayland will be making himself?

A When and as and if this Mayland Refinery is able to produce a competitive standard grade of gasoline, third grade gasoline and one or two of the burning oils, they then would certainly would have to be considered.

Q Speaking about the decreased volume of throughput to the Imperial. He is now buying his first and second structure gasolines from the Imperial. I am only talking now about gallonage. He will presumably replace that at once with his own manufactured product?

A Only if he is able to produce that product. As soon as he is able to produce such a product he must be considered.

Q I am assuming that is what the cracking plant is going down there for, is it not, so that he can make standard gasoline?

A I imagine so, I do not know.

Q That would affect the throughput of the Imperial would it not?

A Yes.

Q THE CHAIRMAN: Dr. Brown, I can quite understand how the witness wants to speak about today, and after all we are only asked to make recommendations with regard to the present?

A Up to date.

Q Yes. But we must not lose sight, after all we have to be realists in some sense, and I suppose we are not asked to make recommendations that will only last for the afternoon and be of value for the afternoon. If it is established definitely that a plant will be, or that another refinery will be in operation in a month, I think it should be taken into account by the witness. I feel this way, that all this piece-meal must, of course, be before us, but ultimately somebody like Dr. Brown, I should think, will have to survey all these things and say "I am competent

to speak and give an opinion, and I offer to this Commission not what is in Exhibit "310" but what should be a fair price for gasoline, or whatever he has considered." These other matters are merely steps by which he arrives at that final conclusion.

MR. FRAWLEY: That is my conception of what Dr. Brown is going to do.

THE CHAIRMAN: All these refineries have to be considered, not just the Imperial picture. The whole subject of capital costs, operating costs and everything enters into it. And if you have a witness who is capable of dealing with all of these factors and then offering an opinion, it would be of very great help to us. Unless somebody does, we will not be making any answers.

Q MR. FRAWLEY: We are stating to the Commission of a plant going into operation in August. Do you feel competent, if you went to the Mayland plant and discussed the whole situation with the refinery superintendent, what he is building, first what the plant is physically and how much it is costing and what his throughput is or he expects it to be and what share of the market he now has, and whether he intends to supply that share of the market with standard and Ethyl gasolines from that plant rather then purchasing it from the Imperial. Could you come to the Commission with a reasonably accurate estimate of what his refining cost will be, say on the 1st of September or the 15th of September, or something of that sort?

A Assuming all other conditions are as they are now.

Q We have what we have now added to what you may learn by inspecting his plant?

A In other words, I could form an opinion as to what his cost would be right now if his plant were in operation?

Q That is it exactly.

A I do not know what is going to happen to the price of crude between now and Christmas.

Q No, that is true. But that much you can do?

A Yes.

Q Could you do that same if you went to the British American plant?

A I think so.

Q And to the Lion plant, which is also building a cracking plant?

A I am afraid I could not do much with the Lion. I do not know.

MR. NOLAN: Then that opinion as to the Mayland operation would be reflected in turn upon the cost of the refining of the other refineries?

THE CHAIRMAN: Quite.

MR. NOLAN: It would all have to be interwoven.

THE CHAIRMAN: Yes, in my view, and I would like the benefit of your view about it, it is a matter of how we approach these problems that are coming to us. We have to consider all of these factors in arriving at some answer that we must give with respect to these things.

MR. NOLAN: This whole discussion at the moment has been predicated upon the assumption that this Commission should recommend a price.

THE CHAIRMAN: Mr. Nolan, that has come up before. We do not think we have any statutory duty, nor any duty imposed upon us by this Commission, which will require us to recommend price fixing, which has been the subject of some comment. Now, whether we do or we do not, we will not say in advance what we may do, but at the moment I am not taking very seriously any talk about price fixing so far as this body is concerned. Nor do we find anything in our Commission that suggests that we can or we should make any such recommendation. I do not say it would be incompetent to us to make it.

MR. NOLAN: No, but what the Commission says is that you be asked to recommend what the fair and equitable price should be. That is all. And that is the beginning and end as I understand it, of the duty of this Commission. But there is in evidence before this Commission this petroleum products price fixing legislation.

THE CHAIRMAN: Yes, you brought that to our notice. I had not seen it before. Therefore, it is not of any weight with us, Mr. Nolan, because it is not directed to us.

MR. NOLAN: One of the bases of this Inquiry.....

THE CHAIRMAN: The Minister has been given certain power, I gather, from a cursory reading of it, to fix prices.

MR. NOLAN: Perhaps this witness in due course will tell us what he thinks about the propriety of price fixing.

MR. FRAWLEY: I was wondering what my friend was getting at. That is a totally different matter.

THE CHAIRMAN: I think that is a very apt remark of yours. I think, perhaps, this witness - and we will be glad to hear him if he feels competent to speak about that. Certainly. I mean do not just assume in the very slightest degree we have adopted some view that we should be fixing prices, or as yet recommending to anyone else that they do. I do not know what legislation, having been actually passed....

MR. NOLAN: At the last Session.

MR. FRAWLEY: My friend should not be nervous at all.

THE CHAIRMAN: At any rate to leave that, what I would like - and this witness seems to be competent to do it, - what strikes me is and no doubt there may be many other witnesses who are too, to take the whole picture and say "My professional attainments and my experience are such that I am able to say to a client that you should not in that territory be paying more or less than so much for a gallon of gasoline, or distillate or whatever we are talking about. I say this witness appears to be a man competent to do that, in the light of his training and experience. If he is, he must take into account every single factor that would lead him to the opinion that he would be able to give or that he did give. Now, Dr. Brown, are you such a person?

A I have had occasion to do things of that kind for different bodies in the States, and I believe that I

could do that in a satisfactory manner, provided the information is forthcoming and that I have time to digest the facts.

THE CHAIRMAN: We are asked to give certain opinions. Now then, if we are competent to do that in our turn it must be because we have had competent witnesses before us who have guided us in respect to professional matters.

MR. FRAWLEY; Quite so.

THE CHAIRMAN: And if this witness is able then, it is the business of this Commission, I think through its Counsel, to see that the material that he requires upon which to found his opinion is made available to him, wherever that may lead him.

MR. FRAWLEY: I am very glad to have Your Lordship's observation in that respect, and I think that will assist me greatly.

(At this stage the Hearing was adjourned until 2 P.M.)

....

[illegible]

2:00 P. M. Session

EXAMINATION OF DR. BROWN CONTINUED BY MR. FRAWLEY

Q MR. FRAWLEY: Dr. Brown, now perhaps there was some misunderstanding; when you went on this morning it was in my mind that you would take these Exhibits which Mr. McGrath put in and just, it was in my mind to have either you or Mr. McGrath review them, but you are on the stand and I thought you might just run over these Exhibits and make them completely understandable to the Commission so that, in the record, so that when they begin to examine the evidence they will have not only the Exhibit in front of them but a detailed explanation in the evidence, in the record, as to what they all mean, so if you would be good enough to do that ......

A I will do what I can on that, if Mr. McGrath will follow me.

Q Mr. McGrath, Mr. Nolan and his other associates can attend and correct as you go along in your answer.

A I am not sure that I have all the Exhibits but I believe the last numbered one which deals with the refinery operation is "300"; "300" refers to marketing cost and "301" refers to marketing costs, I do not believe you wish me to explain those.

Q No, that is right, "300" and "301" go out then.

A Now "302" is the specifications of the products as to the gasolines and casing head and tractor distillates and Imperial naphtha.

Q Marketed out of the Calgary refinery?

A Marketed from the Calgary refinery.

MAJOR LIPSETT: Those three, Mr. Frawley,

are confined to the Province of Alberta, they do not refer to the whole refining, do they?

MR. FRAWLEY: The specifications of the products, these are purely specifications, Mr. Commissioner. Just what the product is and that is all, purely specifications, what the Octane is, what the gravity is, and so on, it is just a statement, it is just a piece of information. Mr. McGrath put it in at that stage because he had been asked to file it.

MAJOR LIPSETT: Exhibit "301" is marketing costs?

MR. FRAWLEY: Yes, but we are dealing with Exhibit "302".

THE CHAIRMAN: You are starting with which one.

A "302" and "303" are really the same thing, they are product specifications from the Calgary refinery. Now I understand that these are specifications which are met by all of the products sold as Imperial products and therefore there is a range given, in other words we find a distillation range and octane range and so on, so that the actual material marketed from the refinery will possibly vary within the narrow limits stated in these specifications. I think there is nothing more to really say about this except that.

Q Why is there no A.P.I. gravity given for standard gasoline for instance on Ethyl gasoline and even third structure Acto gasoline?

A Well gravity is no longer a specification on which gasoline is purchased or sold; in the old days of course gravity used to be the whole thing.

Q I see.

A Now it is octane number and distillation, along with other specifications such as sulphur and corrosion and doctor, just such as those.

Exhibit "304" is a detailed analysis of the manufacturing costs for the year 1938 at the Calgary refinery. Now I might point out there that some of these items will remain practically constant regardless of the amount of crude which is refined. The salaries, I should imagine, represent the permanent staff and would be absolutely constant regardless of how much crude is processed at the refinery. The Items in the red ink indicate credit to the expenditures for salaries which are allocated to the other Departments. The first column in red shows the expenditures for salaries which are credited against the total expenditures because they are allocated to the tank car department and the second column in red similarly, credits against salaries which are properly chargeable to the crude oil shipping expense, as the handling of the crude oil is not, the handling of the crude oil which is sold is really not part of the function of the refining operation but again I imagine that those figures would probably change depending upon the proportionate amount of crude which is run in the refinery to the proportionate amount which is sold, so that the figure $87,973.00, representing manufacturing costs, salaries, might change within narrow limites, depending upon whether or not the crude which is brought into the refinery and sold from the refinery remains constant. I hope you will stop me if

I am misinterpreting this.

Q You are about to leave that item then?

A I thought I should.

Q Let me ask you something, one of the things which the Commission is expected to inquire into is, as expressed in our agenda or our programme under the heading of refining, whether with regard to capital investment, depreciation, operating cost or any other cost , any expenditure is incurred or charge is made which is either wholly or partially unnecessary or is not essential or is not in the public interest; and ~~I merely~~ ask you now in looking at this item of $87,973.92 as an expense, whether or not there is anything which would warrant the Commission in inquiring into the propriety of any of these expenditures or on the other hand do you look at them, are you looking at them and are you satisfied with them without any further detailed analysis of them?

A I am inclined to accept those as being representative of a reasonable expenditure for supervision and general office overhead. As I mentioned early this morning, in the States on a plant processing 5000 barrels we probably would not employ in the refinery as many as five engineers. We might have a few, a smaller number of men drawing those salaries and I indicated that there were reasons for that, due to the fact that in the States many of the refinery operations are adjacent to or in the vicinity of very large industrial centres where they can get the engineering advice and special services and so on, where perhaps a refinery at Calgary has to maintain their staff for that purpose and I believe that the differece in

conditions between these large industrial centres in the States and Calgary will substantially justify, or will justify substantially all of that expenditure.

Q That handicap which you mentioned this morning is reflected there in the fact that they have this greater number perhaps, of men, seven mechanical foremen for instance, would that be an item which would be explained by this lack of being adjacent to a large industrial centre?

A They might be in part explained by that and also I believe this is an old plant, it is not designed as a compact unit and therefore, the maintenance of it may be a little more expensive and they may require a few more men to supervise the maintenance of the different units, than would otherwise be the case.

Q Yes?

A That is a situation that exists and has to be met.

Q That is the situation there and it may not be the time to consider what I am now going to suggest but if that be a fact that more men are required because it is not so compact a unit, or whatever word you used a moment ago, is it possible that that is something which the Commission should write out by virtue, write out of the cost, by virtue of the direction which they have to ascertain whether or not there is any expenditure incurred in the operating cost which is either wholly or partially unnecessary or is not essential or not in the public interest?

A That could be, some of that might be written out if they were considering comparing this plant with a new

modern plant to be built at the present time but at the same time I should point out that in a new modern plant it might require fewer men in the specialized mechanical end and the technical staff, but on the other hand would probably have an appreciably higher capital cost because of the use of special alloy steel and special fittings and so the depreciation would probably be larger and it is my experience in comparing plants of this type, which represent a type of construction of about say 15 years ago, with the modern plants, that usually a careful study indicates that the actual operating expenses of the old plant, are not significantly higher than that of the modern plant. If you were building a plant at this time it means you would build to a modern design but having an old plant in any operating condition, where it is in large part depreciated, so that it has a value on the books of something like $2,000,000.00 where a new plant would have a value of perhaps four or four and a half million dollars, that the increased capital investment in the new plant will compensate for the increased operating expenses necessary to maintain the older plant. Now based on my experience where I found that to be almost always the case, I again say that I think these figures for these salaries are proper, due to the conditions that exist in this refinery and in this part of the country.

Q Now we have not got to the other question then, supposing for instance you went into the B. A. plant and found that their comparable item was less?

A Yes.

[illegible]

Q Then in the end you would, when you make your further submission to the Board, you will take that into account as against this figure here?

A Yes.

Q But at the moment you are simply saying that you think the expenditures which they show incurred in that plant are reasonable and proper?

A For the conditions as they exist.

Q Yes, all right?

A And under wages again, it seems that there are a large number of men employed for the through-put; I believe that indicates that probably about 200 men here are in that refinery, while a modern plant, putting through the same amount of crude in the States would probably in some cases operate in a satisfactory manner with perhaps half that crew, that would be perhaps a small number; again that plant has a larger capital investment and I believe that on the whole, considering conditions as they exist here in Calgary and in this plant, that that is, without doubt, a fair pay roll for wages. It may be possible if they were, if the Imperial were against really stiff competition and they had to curtail, they might find it possible to get along with fewer men, they might even find it possible to operate with lower wage scales, if they could get along without labor troubles, but all of those things are unpleasant conditions to meet and if you overwork the men and underpay them, you are always facing trouble, so on the whole again I feel that those figures are probably fair and just, when all of the factors are considered and the conditions as they now exist.

Q Quite.

A Those two items together, salaries and wages, would probably remain substantially the same regardless of the amount of crude put through that refinery within limits, that is to say if they processed their 4,000 barrels a day or 6000 barrels a day, I believe that those two items would remain practically the same. There might be a slight decrease in the employment of unskilled labor but it would not be significant so that those items are more or less fixed for this refinery when operating within the limits of perhaps four to six thousand barrels a day.

Q Yes?

A The next item, pensions, of course is fixed anyway. That would be a constant amount regardless of the through-put. Now under the item, I might also say that these items on Exhibit "304" are detailed break-downs of Schedule 3 of Exhibit "280".

Q Yes.

A And that the totals shown on Exhibit "304" are the same as those shown on Schedule 3, after making the proper allowance for the allocation of salaries, wages and material, to the tank car department and to the crude shipping expenses.

Q Yes?

A Now as to the repairs, material and supplies, there again there is a figure which perhaps might be larger or might be smaller depending upon the type of plant which is installed and whether or not it is operating to maximum capacity or operating under different conditions, but

that figure again will remain substantially constant regardless of the amount of crude put through the plant insofar as the repair material and supplies are concerned. You will notice that the repair material and supplies shows $134,476.00, I am leaving off the cents, to which is added chemicals of $47,358.03 and the two of those items together make up the total under materials on Schedule 3.

Q Yes?

A Now the chemicals would in turn, of course, be more or less proportionate to the amount of crude run and the repairs would probably be somewhat decreased; those figures seem reasonable considering the plant. It is an old plant and considering the fact that they are really crowding that plant, putting through about as much crude as it can handle.

The other expenses have here been set forth in detail and I believe that those would have to be explained perhaps by Mr. McGrath because they represent certain peculiarities in the set-up of the Imperial Oil Company with which I would not be particularly familiar.

MR. FRAWLEY: I wonder if I might stop you there. If you see no objection, Mr. Chairman, Mr. McGrath might, from where he stands, just deal with that one item and then Dr. Brown can proceed. That would seem to be the easiest way, rather than calling Mr. McGrath.

THE CHAIRMAN: All right.

Q (MR. FRAWLEY TO MR. MCGRATH) Mr. McGrath, you did give us a breakdown of the item, other expense, in Exhibit 304,

$65,101.98, your Exhibit "304" in the costs was the breakdown of that?

A Yes.

Q Some of them are obvious?

A Yes, the first is Workmen's Compensation Premiums, $8,799.70, that was what was paid to the Workman's Compensation Board and the Group Insurance Premium $1,821.32, I cannot say right off hand what that item is.

Q It is an insurance expense?

A Yes, that is right.

Q They probably have a group insurance policy?

A Yes, and death benefits $1,774.80 and Coutts Refinery $3,593.00.

Q What is that?

A That is the watchman at the Coutts plant, because that is shut down and they have the equipment down there and they had stocks at the Coutts plant.

Q Oh, Calgary stocks you might say?

A Yes.

Q At the Coutts plant?

A Yes.

Q So it is charged against Calgary?

A That is right.

[illegible]

J. McGrath

A Engineering Department expense at Sarnia. We have a general Engineering Department there, and that is Calgary's share of that expense.

Q Now you are coming to the other item of the same kind?

A Technical and Research Expense Sarnia. And that is our Technical Research Division, and that is the portion that is chargeable to the Calgary refinery. Each refinery bears a portion of the expense.

Q Is that the same kind of an expense as the item "Engineering Development" in Schedule 2 of $10,507.00?

A Engineering Development generally deals with new equipment. The engineering at Sarnia is just a general engineering department within the Company and deals with changes in plant rather than new equipment.

Q It is an allocated expense, just like the item Administration and General Expense?

A That is right.

Q That is, it is under various classifications?

A Yes.

Q Do I understand that you allocate against the Calgary refinery some of the salaries paid to the technicians in the Sarnia refinery?

A In the General Engineering Department.

Q Which is located in Sarnia?

A Yes. The General Engineering Department of the Company and the same with Technical Research. That is the same thing.

Now contract labor expense is some work that has been contracted, $18,897.98. I do not know what that would be. It probably is dismantling the plant or changes in the plant. Telephone, telegraph, and travelling are self-explanatory.

Q Yes; thank you very much, Mr. McGrath.

DR. G. G. BROWN, recalled:

Q MR. FRAWLEY: In the light of Mr. McGrath's information, particularly looking at the items which originated in the Sarnia refinery and then the further item........ well, you have not come to that though. Just dealing with what has been broken down by Mr. McGrath just now, what are your observations?

A The items referring to Sarnia, as I interpret them, they are a charge against the Engineering Development and Technical Research which is conducted at Sarnia for the Company, in which all of their refineries share.

MR. MCGRATH: That is correct.

A In other words, you might say that is an expense item in order to keep the Company up to date in their processes and their methods of treating crudes. It is the practice in the States to frequently employ a research company to do that. For instance , I am associated with the Universal Oil Products Company, which builds plants and charges a royalty for the operation of these plants, which royalty is spent in research and development. It happens now that that charge amounts to about 10¢ a barrel on the amount of crude oil sent to the cracking unit. This figure would correspond approximately to 10¢ a barrel for each barrel of crude run through the stills in the Sarnia refinery. So that this is in many ways comparable to what a small refinery, or a small independent refiner, might pay as a royalty in order to ensure his getting the benefit of all modern developments. It seems to me that might be regarded as comparable to that.

Q It is a proper charge, then?

J. McGrath
G. G. Brown

A I think it is a very proper charge under these conditions, because I understand the Imperial does not operate any licensed processing. They are all processes which are free for your own use or owned by yourselves. Fuel. Still gas. Refinery production represents the value placed on the gas produced in their cracking operations and used as fuel. In other words, it is gas which is the product from the petroleum and has a value and might be sold as fuel. But it is consumed within the refinery and therefore is a proper charge to operating costs providing that it has been duly credited to the operations in the production of the materials from crude, and I understand that it has been so included.

The next item, natural gas, represents just as it says, some outside gas which has been purchased and used as fuel in the operation of the refinery. And also the $95,000.00 to Royalite, purchase of gas.

Q May I stop you there, please, Dr. Brown, and ask Mr. McGrath if he can tell us why some of the gas is purchased from the gas company and some from your own company?

MR. MCGRATH: (Recalled) You asked me, Mr. Frawley, how the invoices were made out, and I state that is the way the invoices were made out. It was part made out to the Canadian Western Natural Gas Company, and part to the Royalite.

Q Do you know whether you paid the same price to each company?

A There is a 9¢ price per thousand.

Q So much to the Canadian Western Natural Gas Company?

A Yes, and so much to the Royalite.

G. G. Brown

Q Do you pay 9¢ to the Royalite, too? Well, perhaps I should not be bothering you, but I wonder if we should not have some schedule showing how these were made up and the prices they are made up on. One may be unscrubbed and the other scrubbed?

A It is the same gas entirely. But I think part of the payment is made to the Gas Company and part to the Royalite Company.

Q In other words, you are purchasing the same material from the Gas Company and some from the Royalite?

A It must be.

THE CHAIRMAN: It may be the same per cubic foot?

A Yes.

Q MR. FRAWLEY: That is, you think you are paying the same per cubic foot?

A We pay 9¢ a cubic foot for the gas. That 9¢ is divided between the Canadian Western Natural Gas Company and the Royalite Company.

Q THE CHAIRMAN: Do you know what the Canadian Western Natural Gas Company is getting?

A $27,000.00 and the Royalite $95,000.00.

Q MR. FRAWLEY: I wonder, is there any transportation in there?

A I will find out for you definitely what it is.

Q If these were broken down, we might find that you were paying one price to the Gas Company and one to the Royalite?

MR. MCGRATH: Does the Gas Company transport the gas?

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G. G. Brown

Q Yes, they do. They have their own special pipe-line.

A That probably covers transportation and the other covers the price of the gas.

MR. FRAWLEY: That may be just simply a transportation charge to the Gas Company and for the product itself to the Royalite.

A It looks as though it is divided 2 to 7.

Q However, you will explain that to us.

DR. G. G. BROWN, recalled:

Q MR. FRAWLEY: Then, Dr. Brown?

A This item "Fuel" is another item which would vary about proportionately to the amount of crude being run by the refinery, and the same statement will also apply to the next item, "Electric Power, City of Calgary". The more crude being run, the more power will be consumed. The last item, "Engineering Development", is something with which I am not specifically familiar. I imagine it is the engineering development at Calgary.

MR. MCGRATH: No, it is Calgary's share of the engineering development, of the total engineering development, charged to Imperial from the Standard Oil Development Company. In other words, the Standard Oil Development Company billed the Imperial with a certain amount of money, and this $27,000.00 is Calgary's share of that.

MR. FRAWLEY: Thank you very much. Does that make it perfectly clear?

A I understand.

Q Nothing you want to ask Mr. McGrath about? What do you say about that then?

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G. G. Brown

THE CHAIRMAN: We have engineering expense at Sarnia and engineering development, is that something different?

A I understand this is a development charge that goes back to the Standard Oil Development Company. It does not go to Sarnia.

MR. MCGRATH: No, that is where it originates, the Standard Oil Development Company.

MR. FRAWLEY: Which is a subsidiary of the Standard Oil of New Jersey Company, as I understand

A This again is in the same category only it goes to a different organization.

MR. MCGRATH: It covers a wider field. The developments are far greater in that field than in the Sarnia General Engineering.

A That again is one of the items which these large companies carry and sometimes the independent refiner ducks. If he is successful enough to get the benefit of modern improvements without paying for their development, why, he is so much ahead. It is one of those things that has to be borne by the industry as a whole and in the larger companies they prefer to do it in their own organization, while in the smaller independent companies they frequently wait until the development is made and then get the benefit of it by some license or royalty agreement. That is a matter of policy for the various companies to decide. In the long run, I imagine it is pretty near a wash-out or a balance.

Q What would you say if you added together the items $17,624.66, being engineering expense, Sarnia, and the

G. G. Brown

item $2,457.89, being technical and research expense, Sarnia and the item $27,105.07, being engineering developments, this being to the Standard Oil Development Company. What do you say, when you put them all together, as to how much per barrel it is and how it would compare to this amount you say the independent refinery in the United States pays by way of royalty?

A I think it is quite a bit less than the independent man would pay. This total here of approximately $47,000.00 which would be distributed over approximately 2,000,000 barrels. Call it 2,000,000 barrels. Is that right?

MR. MCGRATH: That is right.

A It amounts to about 2½¢ per barrel of material put through the refinery and approximately 40% of the crude would go to the cracking coils, and that would mean, if it is 2½¢ per barrel on crude, it would correspond to just about 10¢ per barrel of material to the cracking coil.

MR. MCGRATH: About 6¢, Doctor?

A Yes, beg pardon. Corresponds to about 6¢. Correct that, please. Corresponds to about 6¢ per barrel of material fed to the cracking coils. Now, the small independent operator will probably pay a royalty of about 10¢ a barrel on all materials to his cracking coils in order to get the benefit of the corresponding development. So that the large company by absorving the expenses for developing new operations and keeping up to date, is in the long run probably able to get the benefit of modern improvements at a lower cost than is the small refiner who waits until the process is developed and then pays a royalty for its use.

G. G.BBrown

So that these costs would correspond approximately to what the independent refiner would have to pay as a royalty. They are a little bit less.

Q That completes Exhibit "304", does it not?

A Yes. Now Exhibit "305" is a further analysis of the credits shown on Schedule 3 of Exhibit "280", which are shown as "Less Miscellaneous Revenue $36,321.00".

Q THE CHAIRMAN: Dr. Brown, before proceeding, taking it as a whole, does it strike you that this is a large operating expense for a plant of the size of this plant, an operation of the capacity of this plant?

A You mean these figures as shown on Schedule 3?

Q The $962,000.00 or nearly $1,000.000.00 operating a 6,000 barrel refinery?

A The figure that you have reference to is on Schedule 3.

Q Exhibit "304", just before we left it. It is the item of $962,917.60?

A Well now, that expenditure, and the total of that column you have just given me, is the total expense, not including depreciation, and taxes, is that right?

MR. MCGRATH: Yes, and administration.

A And administration, which is not in that figure. Also it included certain items such as credits Tank Car Department, Shipping Expense, Sales of other materials. So that that figure of $962,000.00 does not truly represent the expense of operating this refinery on the crude which was refined. That figure is given more accurately in Schedule 3 of Exhibit "280" which gives the total manufacturing costs,at the bottom of Schedule 3 of Exhibit "280".

Q Yes?

G. G. Brown

MR. NOLAN: The last figure there?

A Oh, yes. $935,000.00 is a figure very similar to the one you mentioned but it does give the total manufacturing costs, after including depreciation, taxes, and all of the other credits.

Q THE CHAIRMAN: Yes?

A As I indicated before, it appears that the costs in a location such as Calgary and Canada are somewhat higher than the refining costs or the expense in the United States, and from that standpoint, the figure looks a little high to me.

Q What would you have to say about a plant of this size, that is comparable, what would it operate for in the United States?

A A plant operating at capacity and having approximately the same storage problem, and running 6,000 barrels a day, he would have an operating cost of about $2,400.00 or $2,500.00 a day. A little bit more than that. That would be a rather low figure. That is about it. It comes pretty close, does it not? $2,400.00 a day, 365 days, is about $875,000.00. Is that correct? Check that. I should imagine a plant, a modern plant, doing about the same job, and having the same storage problem, might be able to operate very satisfactorily at $875,000.00 a year, as compared with this $935,000.00, which I think is about the same difference that I indicated before. So I feel after taking the whole thing into consideration, that the operating expense and cost would be regarded as reasonably satisfactory. In other words, after they get their new plant in and operating, aside from the savings

[illegible]

in the Ioco naphtha which will not have to be used, their figure will be probably very comparable to this, when all factors are considered.

Q We have not heard about the new plant yet, have we?

MR. FRAWLEY: No, we have not had anything in evidence about the new plant. Dr. Brown can probably tell you. It would not be evidence but perhaps before we leave it, he will tell us something about it?

A My statements here are getting rather confused as to what are facts and what are opinions. I hope the record will be reasonably clear on that.

THE CHAIRMAN: We are accustomed to that.

A This $875,000.00 is an opinion. Although within the last two years I have had occasion to make an economic analysis of plants running from about 5,000 to 10,000 barrels in a number of cases, and I do feel that that figure is a reasonably sound one.

Q Speaking in a very general way, you feel that this operating expense which is claimed is a reasonable one?

A Yes sir, that is, taking the conditions as they exist at this time.

Q MR. FRAWLEY: Would this be the proper time for you to discuss the operation of bringing over Ioco naphtha as a necessary part of this refining operation? It is not on that schedule, but it may as well be discussed now?

A I can do that in a general way, I do not have the figures right here that I used in making that study, but if there had been a modern plant in operation - by modern plant I mean one of the newer types of design, with pipe stills

instead of the continuous shell still battery in the Calgary refinery of the Imprial Oil during the past few years, I believe they would have found it desirable not to bring in Ioco naphtha, for the reason that they would be able to get sufficient octane number out of their cracking plant. But because they were cracking more severely, the recovery of gasoline and other liquid products from the crude would be less, so that they would have to run more crude in order to get approximately the same yield, which means that they would take an additional loss on the processing. I made the best estimate I could of that loss, and it appeared to be that there was just about an even break between bringing in this Ioco naphtha, which costs something around 14¢ a gallon, 14¢ plus I believe, and selling it in the gasoline at about 8.64¢ a gallon throughout, and taking an apparent loss of about 5½¢ or 6¢ a gallon, as compared with taking an additional run of crude and getting less recovery. It looked to me at first as though, and I think I mentioned it to Mr. Frawley, that it was a kind of a weird thing to do to bring in this Ioco naphtha, but when I started to figure it out, it did not look so weird. It really indicated it was the best solution to the problem that the Imperial had to meet at that time, which was to produce a gasoline of a high octane number to meet a competitive standard, such as indicated in these specifications, and this seemed to be the most efficient way to do it, was bringing in Ioco naphtha. Although it might appear odd on the face of it, it is on a careful analysis really the economic way of meeting the requirement.

G. G. Brown

Q. MR. FRAWLEY: Then it would appear that the installation of the new plant is not merely to obviate the necessity of bringing in that Ioco naphtha?

A I do not know what is in the minds of the Imperial Oil Company, what their reason is for building the new plant. But as I studied the situation, it would appear to me the real reason for building the new plant is to get a plant of sufficient flexibility so that they can meet all competitive conditions they may have to face within the next few years. And also that the present plant is getting old and the expense of maintaining it is high, and perhaps it is about time to replace the old plant with a new one. Taking all these factors into consideration, it seems like a wise move to put in a new plant. I really believe with the new plant that the operating costs over all will not be greatly reduced. In other words, it is an investment which is made largely not from the standpoint of getting a rapid return on the investment but for the sake of being able to give the proper service and maintain a competitive condition with a more flexible plant. That is my opinion that I have arrived at from studying the situation. It may be there are some other reasons in the minds of the Imperial Oil.

THE CHAIRMAN: Are we going to hear evidence about this new plant? I mean to say, if we are going to take into account the operating costs of the old plant and the depreciation that still attaches to the old plant, and the fact is that the old plant is to be scrapped and a new one set up, perhaps we should hear about it? Perhaps that is what we should be hearing about.

G. G. Brown

MR. FRAWLEY: We cannot hear much about it yet, of course. It is just in the blue-print stage down in Toronto some place now. So far as I know, it is. Certainly, the ground has not been broken.

MR. COTTLE: The ground has been broken.

MR. FRAWLEY: Then it is one step further than the blue-print stage in Toronto.

THE CHAIRMAN: What happens? There may be nothing in this. But I do not understand. You have a plant, we will say for the reasons which the witness gives, it is considered desirable to scrap it, and set up a more flexible one. That plant has been paid for presumably out of operating expenses. Putting up a new one of great value, we start all over and depreciate. Has that any bearing on the Inquiry we are concerned with?

MR. FRAWLEY: Perhaps I could let Dr. Brown answer that.

THE CHAIRMAN: I would like to know.

MR. FRAWLEY: It is this year's Commission and not next year's. We have to take what we have, and that is the 1938 operations, which is on the old plant. If we adjourned for twelve months, we might have a 1939 operation, which would be, in part, we do not know how far, and we have no idea at all how soon the new plant will be functioning if at all.........

THE CHAIRMAN: I suppose he is entitled to say it might never be gone on with. But supposing it is proven to us by a competent witness who is able to speak for his company, that this plant is to be scrapped in the near future and a new one set up. Has that any bearing, or has it not?

G. G. Brown

MR. FRAWLEY: My submission would be, just at the moment, Mr. Chairman, that it has nothing to do with your task of analyzing the operations of this company today.

THE CHAIRMAN: With this plant?

MR. FRAWLEY: With this plant, because I think the other thing is not only conjectural, but it throws us away into the future because we have to think of how soon the plant will be completed and how soon it will be functioning. Secondly, whether it is a complete replacement. As I understand, it is only a replacement in part.

MR. NOLAN: That is right, only in part.

MR. FRAWLEY: So that we would have part of the present plant operating.

A I think perhaps that is a little confusing due to the way I have made my statements. I have not sharply differentiated between what is facts based upon the 1938 history and what is perhaps my opinion. I want it understood that any statement that I have made as to comparative costs of this operation of 1938 and the comparative costs of the operation in the States, and comparative cost of any plant that is not now in existence, is a comparison of facts on which we might place a great deal of confidence, and simply an engineering estimate which has been rather roughly prepared while I am on my feet, and in which I have considerable confidence, but nevertheless, it is still an estimate. I have been studying this thing primarily from the standpoint of history,

G. G. Brown

that is, the 1938 operation. We have a good deal of certainty that these figures are correct. Now, I think it would be desirable if we are going to study or make any estimates as to what might happen in the future that we perhaps keep that separate from the discussion as to what has happened in 1938.

THE CHAIRMAN: Well, I do not know, we have had one experience with history. We might not, I do not know, be content to rely entirely upon history.

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If it were established to our satisfaction by someone that a plant set up today, although I do not gather from your evidence that you would subscribe to it under the circumstances that exist here, but if it were established to our entire satisfaction that a plant set up today would operate at a manufacturing cost of 20 cents a barrel less, I do not know, Mr. Frawley, that we would take the history of Imperial and say to His Honour, the Lieutenant Governor, that the price should be based on that historical situation, not for a minute.

MR. FRAWLEY: No, with that I agree.

THE CHAIRMAN: What a new plant not in existence might do----

MR. FRAWLEY: Or what a plant like the British American, which is in existence but which is just new, might do or is doing.

THE CHAIRMAN: Quite so.

WITNESS: Do not misunderstand me, I did not mean that that should be excluded; what I meant was that, it was confusing perhaps to mix the discussion of the two things at the one time as I unfortunately have been doing, I am talking about the future and the past at the same time and it may be confusing.

Q. MR. FRAWLEY: I thought we understood, but at the moment we tentatively, at least, have decided you would study the British American operation and the Mayland operation and the Lion operation and then come back with a statement to the Commission.

THE CHAIRMAN: And if it was thought proper----

MR. FRAWLEY: The new British American.

THE CHAIRMAN: What a plant wholly different

... it were [illegible] ...

that a [illegible] ...

from your [illegible] that you would [illegible] ...

this [illegible] ...

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

that [illegible] ...

[illegible]: [illegible]

THE C[illegible]: [illegible]

[illegible]

[illegible]: Or [illegible] ...

[illegible], which is in [illegible] ...

now, [illegible] ...

[illegible]: [illegible]

[illegible]: [illegible] ...

did not mean that [illegible] ...

that, it was [illegible] ...

was [illegible] ...

[illegible], I am [illegible] about the future [illegible] the past [illegible]

[illegible] ...

[illegible]: [illegible] ...

the [illegible] ... you would

[illegible] ...

[illegible] ...

[illegible] the Constitution.

[illegible]: [illegible] ...

[illegible]: [illegible] ...

[illegible]: [illegible] ...

from any of them might do under the circumstances.

MR. FRAWLEY: Yes, I see.

THE CHAIRMAN: I mean, I do not know where this evidence will lead us, but this is what I would like to get and which would permit of this Commission doing what it thinks wise, just in the end, in the way of recommendations, evidence upon which we may act here, not one theory ridden to death and others discarded, because that which is thought wise by one person may not be accepted by us.

MR. FRAWLEY: Quite.

THE CHAIRMAN: If we have them all then, using our best judgment, we can adopt one method or another as the case may be.

MR. FRAWLEY: Yes.

THE CHAIRMAN: But to the extent you as Commission Counsel think any method should be thought of, we would like to hear about it, because at this moment we certainly have no fixed views as to what our approach to this problem will be, much less where we will end.

MR. FRAWLEY: I have a very definite idea at the moment as to what this further study is that Dr. Brown is going to make.

THE CHAIRMAN: Well having interrupted so much, we will try and let you go on in peace now.

Q MR. FRAWLEY: You were about to discuss Exhibit "305", Dr. Brown?

A Now "305" is a further analysis of the credits of the operating expenses shown on Schedule 3 of Exhibit "280", miscellaneous revenue, some 36 thousand dollars. I frankly cannot explain those beyond what it shows on the sheets.

MR. FRAWLEY: Perhaps Mr. McGrath will help you out there and just explain Exhibit "305", Mr. McGrath.

MR. McGRATH: Well the rental revenue is the rental for the crude tanks and the next employees' garages, the next item the sale of scrap material and the next item, is miscellaneous sales of material and supplies, that is all.

MR. FRAWLEY: The big item is the amount of $23,333.28, which I understand is what you receive from the Royalite for the tanks which it rents from you in the Calgary Refinery yard.

MR. McGRATH: In 1938, that is right.

MR. NOLAN: Did rent.

MR. FRAWLEY: Did rent in 1938.

MR. McGRATH: Yes.

MR. FRAWLEY: Well then the other is just a sale of material, does that explain that, Dr. Brown, is that sufficiently explanatory for you?

A Yes.

MR. FRAWLEY: Now I want to be clear whether it is worth while inviting Dr. Brown's opinion as to this tankage rental, it is of no consequence now.

MR. NOLAN: It is of consequence because there is no credit in 1939.

MR. FRAWLEY: Yes, this is a credit which we find in 1938, it is there in any event, the Imperial received that rental from the Royalite and that rental will not be paid in 1939 probably.

A Well it is really what we call a non-recurring income, is it

not, an incidental.

Q It is not very large in the over-all operating costs, is it?

A Well it is not really part of the operating costs, it is taken out of the operating costs, a sort of credit for some service furnished by the refinery department.

MR. McGRATH: It reduced the cost.

MR. FRAWLEY: Yes, it reduced the cost in that amount.

A In that amount and I think that is about all that can be said about that.

Q MR. FRAWLEY (TO DR. BROWN) The operating cost has got the benefit of that for 1938, even although it does not get it again?

A Yes.

Q Then Exhibit "306"?

A Exhibit "306" is a further analysis of the administration and general expense items shown on Schedule 3 of Exhibit "280".

Q Yes, now?

A And it is classified into a number of different kinds of expenses, those which are direct and pro-rated according to the crude run and pro-rated according to the plant investment; that is any general expense which is incurred by the main office in Toronto which has been pro-rated to the Calgary Refinery again, is somewhat in the same category as the research development and engineering expenses, which are to be paid for by some means.

Q Well to put it to you very bluntly, do you think that this company, if it were purely an Alberta organization, carrying on this sized operation, would have in its operating costs,

this item of, I do not know how much to take, but take the whole $67,000?

A No, in my opinion if this refinery in Calgary was a local organization operating solely in Alberta, it would not have as much expense as this for general administration overhead; some of these items would of course have to be covered; on the other hand the sales efforts which would have to be exerted by the Calgary refinery, if it were operating solely in Alberta, would be considerably more than this and we would find a greater cost due to more advertising expense and further sales effort. In analysing the expenses of the refinery I can find nowhere any sales expense and there always is a sales expense; frequently it runs as high as four or five cents a barrel of crude.

Q Let me stop there so there will be no confusion, you mean sales from the refinery?

A That is right.

Q As you understand, the refinery only has two customers, the jobbers and the marketing department of the company, that is right is it not?

A I am not sure. I have not made an investigation of that but I will take your word for it.

Q Assuming with me they have just two purchasers, what they sell to the jobbers in tank car and what they sell to the marketing department, and let us call that a sale, because you have indeed treated it as such, you have treated it as though they were selling at the refinery door, at this 8 cents plus?

A Yes, yes.

Q As to the marketing department and to the jobber?

A Yes.

Q But what you say you do not find, and that is interesting, you do not find any sales expense, the refinery is not charged with, and the refinery is not carrying, any expense of selling this in tank car quantities at the refinery door?

A I see no item in the expenses here.

Q And I think that can be confirmed, that there is no such item?

MR. MCGRATH: No, there is not. Once it is loaded the responsibility is ended.

MR. FRAWLEY: There is just a loading expense at the refinery?

MR. MCGRATH: That is right.

MR. FRAWLEY: Into the cars for the jobbers and for the marketing department?

MR. MCGRATH: That is right.

Q (MR. FRAWLEY TO DR. BROWN) But outside of that there is none of this other expense you spoke of?

A Now a small independent refiner operating one unit will always have a sales expense to keep their product sold to the jobbers.

Q Yes, I see what you mean?

A And it will be handled in a number of different ways but it is a very real item and I have always had to consider it in these estimates which I have made in the States and I have looked upon this item as compensating in large part for what would otherwise be, you might say, the sales expense and expenses to maintain good will.

Q And where is there any expense, let us analyse that, you have not particularly informed yourself with regard to the

jobber operation?

A No, I have not.

THE CHAIRMAN: Is it clear that it does not come under the marketing expenses, with which we will later deal?

Q MR. FRAWLEY: How about that? Is it clear that this thing you cannot find is not in the marketing expenses?

A It may be.

Q THE CHAIRMAN: Carried into marketing?

A It may be in that.

Q MR. FRAWLEY: Let us see if it is?

A What I have in mind is this, supposing a local refinery, operating as the Imperial is in Calgary, they will have to sell their products to jobbers and there is a sales effort, a sales expense involved in selling their product to the jobber.

Q Yes, now let us be clear that we are all talking about the same thing, and I will ask Mr. Nolan to check me if I am wrong, I will put to you very briefly what the refinery operation is so far as sales is concerned, there is first the gallonage which goes out, not invoiced or billed at all, simply billed at so many gallons to the various marketing outlets?

A That is right.

Q That is about half of the gallonage?

A Yes.

Q Then there is what is sold to about four or five companies, which we call the jobbers, the North Star Company, the Canadian Company, the Union Company, the Maple Leaf Company,

and the McColl Frontenac, perhaps five?

A Yes.

Q Now you say you found nothing in the refinery expenses to take care of the selling effort that there may be to sell that gallonage to the North Star Oil Company?

A Or to any of the others.

Q Or to any of the others?

A Yes.

Q And you think there is some expense in the making of that contract, if I can put it that way, the making of the contract between the Imperial and the North Star, which you would expect the refinery to bear, it is an annual proposition, you see, Dr. Brown, the North Star for instance has been buying, you can take it from me as a fact, its requirements from the Imperial for some years past, no change whatever, year after year they buy their requirements from the Imperial and the same with the Canadian, the same with regard to the McColl Frontenac and I might put to you, and assuming with me it is a fact that the Union Company did make a change quite recently, they brought their gasoline from Ioco by tank car and then distributed it and now they have an arrangement, they are just a jobber now like the others I have named, taking their requirements from the Imperial refinery, now assuming those to be the facts of these jobber operations, would you expect that there would be very much sales expense on the part of the refinery to effect those contracts?

A Well if there is any other source of gasoline that might be brought into this territory either from Montana or Ioco or anywhere else, this other supplier of gasoline would

normally be seeking markets.

Q Or the other refinery, the other sizeable refinery?

A The other supplier or refiner of gasoline, would normally be seeking markets and he would send salesmen in to talk to these jobbers and try and get their business; in other words there is a situation of competition.

Q Yes?

A And to match that the Imperial would have to keep contact with its jobbers and keep them sold by various means; I do not know what effort is being expended up here, I imagine there is much less needed than it would be in some parts of the United States but nevertheless there would be some effort that would have to be expended.

Q THE CHAIRMAN: Would that be a refining cost, would that not be a marketing cost?

A Well take a refinery that does not have any outlets at all of its own, sells wholesale through jobbers, it still has a marketing cost and the cost of effecting its sales to the jobbers.

Q MR. FRAWLEY: A sort of refinery sales manager, that is the gentleman that would do this business, a refinery sales manager?

A Yes.

Q Now there is no such person in the Imperial organization as I understand, that is what you say, you did not find any?

A I see no allocation certainly for that purpose.

Q That is it?

A Now it would appear to me that the Head Office at Toronto would carry on a general sales campaign and in a way would help any one of its refineries in various parts of the

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Dominion to market their product to the jobbers by means of the good will and the general impression that people have of the Imperial as a fine gasoline and so on and that this item is in part at least compensation for what would otherwise have to be in the picture as sales expense.

Q Now of course the gasoline that the jobbers buy, loses its identity as Imperial gasoline immediately it moves away from the refinery door, you understand that?

A Yes.

Q But you still say there would be some selling effort required to keep these contracts alive?

A I have never seen a case where there is not some selling effort required to keep the product sold to the wholesale distributor.

Q Then if I may put it to you, there is no selling effort required within the four corners of the Province of Alberta to keep these contracts alive, would that make any difference, that the arrangements are all made in Toronto?

A That would be exactly what I am speaking about; I did not know what the arrangement was but it ----

Q Assuming with me that that is so?

A If there were such an arrangement, that would be exactly what I am trying to say, not knowing that there was such an arrangement; in other words that this expense in part would at least compensate for what would otherwise have to be included under the refinery expense as a sales expense.

Q Then just to be extreme about it, I put it to you if we had not $67,000.00 but the maintenance and the upkeep and salaries of a refinery sales manager in the refinery in Calgary ---

A And his staff.

Q Would that meet that requirement?

A That would be almost exactly the same as I had in mind. I do not say the sixty seven or sixty eight thousand dollars can be wholly justified on the basis of that sales expense but I think a part of it is equivalent to the central engineering and research and we all know that these large companies with executive offices at some other place in the Dominion, have additional overhead to maintain those offices; now the question is whether or not that additional overhead justifies itself in eliminating what would otherwise be a cost of operation and I feel that in part at least this figure would have to be included in refinery costs as sales expenses if there were no such central office.

Q Yes. Well now I presume that what we have to do is weigh the advantages of being a part, what we have to try to do I presume, Dr. Brown, is to think of the Imperial Oil in Alberta as a separate thing?

A Or set up some independent plant which would be a separate independent thing and have that as a standard of comparison.

Q Yes, and we have to compare that with what the picture is, namely the Imperial merely a part of the whole Imperial organization extending all over Canada?

A That is right.

Q And you have given what might be called some of the disadvantages of the big company?

A That is right.

Q As against the advantages which come from that, and they are what?

A Well you mean the advantages of this?

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Q The advantages that come from being a part of the big organization?

A Well I feel that a good part of what would otherwise have to be included as sales expense is carried by the central offices in Toronto.

Q Yes, we, we already pay into the refinery cost for engineering development expenses?

A That is right.

Q Can you think at the moment of anything except refinery sales promotion?

A Yes. This hearing is an example, most of the men here representing the Imperial are from Toronto and otherwise it would be part of the staff of Calgary that would have to be here, that is public relations and things of that kind are also carried by the central office in Sarnia or Toronto. There are a lot of those things which come up and I am not prepared now to say that $67,000.00 is exactly balanced by some other operation.

Q You have indicated anyway a line of investigation that might be pursued, accounts, I suggest another one to you, that a lot of accounts are carried, the mere fact that Mr. McGrath had to come from Toronto to explain all this indicates that there exists an accounting expense arising out of the Calgary refinery which is carried in Toronto?

A Yes.

Q And I presume is necessarily reflected in these costs?

MR. MCGRATH: Yes, the Calgary refinery bears $10,000.00 of the general manufacturing expense. Now here are items I would like to call your attention to.

MR. FRAWLEY: It may be a good time for Mr. McGrath to deal with the items in Exhibit "306"

and the basis for them?

MR. MCGRATH: Yes, the general purchasing department, Toronto, we have a general traffic department that mass the buying and are able to buy to the best advantage. Now if Calgary was conducted as a separate unit I daresay they would have to have a purchasing expense and probably could not take advantage of price situations and the market as a general purchasing department does in Toronto.

Q Yes?

A General Traffic Department handles the movement of all cars and I daresay if they were not there you would have to have probably a man or so here in Calgary for the movement of cars.

Q MR. FRAWLEY: Yes.

MR. MCGRATH A general manufacturing department, $10,000.00. Now that is part of the movement of all refineries combined, that is Calgary's share of it, $10,000.00.

MR. FRAWLEY: That is -----

MR. MCGRATH: Now, the general manufacturing department, that is Mc. McCloskey's department.

MR. FRAWLEY: And you allocate to the Calgary refinery $10,000.00 of that general manufacturing expense.

A That is right.

MR. FRAWLEY: Which you say obviates the necessity of any of it being carried here at all.

MR. MCGRATH: If you had a separate organization here instead of having one organization for

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all refineries, I am sure your expense would be this high or higher.

MR. FRAWLEY: Yes.

MR. MCGRATH: In the Accounting Department.

Q That is the same sort of thing?

A Yes, here is a technical service, now Dr. Brown spoke of sales, here is a technical service, we have technical men throughout the field contacting the customers, particularly the mines and factories and all that sort of thing, technically trained men and they contact and help them out with their problems and that is Calgary's share of the technical, Calgary's share of the technical expense.

Q THE CHAIRMAN: Taking into account the mere fact that you mentioned mines, am I wrong in suggesting that that perhaps is a man required to promote the sale and contact the purchasers of specialized products, lubricants and greases and that sort of thing, all you sell up here is gasoline and distillates really?

A No, the lubricating oils, greases and that, used in mines.

MR. FRAWLEY: Oh, yes.

MR. MCGRATH: Factories and so on.

MR. FRAWLEY: But the Calgary refinery --

MR. MCGRATH: For instances, tractor trouble, this man would go out on tractor trouble, if a farmer was having trouble with his tractor, they could call in these men and try and solve their problems for them.

MR. FRAWLEY: That is in connection with the motor fuel used in the tractors.

MR. MCGRATH: Yes.

MR. FRAWLEY: Yes, I understand the point, all about the basis of allocation?

MR. MCGRATH: Well all these items marked "A", there are very few of them, only a matter of a few thousand dollars.

MR. FRAWLEY: Yes?

MR. MCGRATH: They are charged direct, it shows right on the bottom here and "B" is the basis of plant investment, that is taking the investment of all our refineries, all the items marked "B", on the basis of plant investment and "C" is on the basis of barrels of crude run. Now if Calgary ran 10% of the entire crude run for the Imperial they would share 10% of this.

MR. FRAWLEY: Of these technical services apparently?

MR. MCGRATH: Yes.

MR. FRAWLEY: There are only two or three?

MR. MCGRATH: Yes.

MR. FRAWLEY: All right for that, anything more you wish to say about the justification of that?

MR. MCGRATH: No, that is all.

Q (MR. FRAWLEY TO DR. BROWN) Now, Dr. Brown, what do you think about the Exhibit "306" in the light of what Mr. McGrath has said?

A Well he has elaborated on the idea that I had expressed rather inadequately, it is the case in a competitive industry as to whether or not this overhead or central expense more than justifies itself. If it does it means that the large company with the central offices can operate more efficiently than the smaller refiner who does not have that central office

and if it does not justify itself, it means then the small refiner without that overhead can operate more efficiently.

Q What does it represent, what does the sixty-seven thousand, nearly sixty-eight thousand dollars represent per barrel of crude refined?

A Well on the crude which they refined themselves it would be about, two million barrels, that is about, something like 35 cents, 3½ cents, is it not about that?

Q About 3½ cents?

A No I did that ----

MR. MCGRATH: 3.35.

A Yes, 3.35.

Q Per barrel of what?

A Per barrel of crude.

Q Refined?

A That is right and if we were to add that in to the other items which were charged against Calgary for engineering development and research, which total more than $47,000.00 --

Q Yes?

A We would still be under what the independent refiner has to pay to get his technical service alone, so that again it is a case of which is the more efficient proceeding and it looks as though it is fully justified.

Q All right, Exhibit "307"?

Q MAJOR LIPSETT: So far, Dr. Brown, your views about it being that that is properly classified as a manufacturing expense?

A Yes, let me explain that a bit by taking a case which comes up quite frequently in the States and I imagine it does here, the refinery is selling motor fuel to jobbers, the jobber

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sells the motor fuel to the ultimate consumer and the driver of an automobile using this gasoline gets into trouble, he has a sticky valve, he goes to the garage and the garage man says "Your gasoline is no good", he goes back to the distributor and tells him that the gasoline is no good and the distributor goes back to the jobber and the jobber goes back to the refiner.

(Go to page 9009)

Now I have had occasion to do that myself for a number of those independent companies who did not have adequate technical services were up against that problem and I know it is expensive and I know it has to be done in order to maintain their markets. Now that is one of the things that a refiner would have to do even although all of his gasoline was sold at his gate to jobbers. It is a burden that he has to assume, to keep the markets open for his products and I believe it should be handled as a refining expense and it always is so handled in making these analysis in the United States; that technical service is exactly one of those items.

Q And you think that should come under manufacturing rather than marketing, do you?

A Yes, because such a refiner has no marketing organization at all. He does not market gasoline. He sells it to all comers who come to his gate to get it. "Marketing" is a term used to get the gasoline and other products into the hands of the consumer. Of course it might be classified somewhere else, but that is usually classified there because any refiner would have to assume that burden even although he had no marketing organization and in my opinion it is very properly chargeable to refining cost as it has been here.

Q MR. FRAWLEY: Yes, now Exhibit "307" do you desire to pass that up?

A Exhibit "307" is a statement of the general administration for marketing, The thing we were just discussing, and that is not part of the refining and therefore I think we need not discuss that any further.

Q MAJOR LIPSETT: Perhaps just before you pass on, I notice now between Exhibit "280", Schedule 3, and Exhibit

"304" and "306", that you first of all have in Schedule 3 of Exhibit "280" an item for $27,105.07 for engineering development?

A That is right.

Q And then when you come to Exhibit "304" you have engineering expense, Sarnia, $17,624.66 and technical and research expense, Sarnia, $2,457.89?

A That is right. Now those item ----

Q Just one more, then when you come to Exhibit "306" you have technical services, apparently at Toronto, $11,397?

A That is right. Now you would like me to differentiate between those and show where they appear?

Q I would?

A On that Schedule 3----

Q And also express your opinion of them, Dr. Brown?

A All right, I will see if I can do that.

(Go to number 9011)

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Q MR. COMMISSIONER LIPSETT: Perhaps you would like to take a note of it?

A I think I can do it just as well now, if you will interrupt me if I get off the track. I think I can do it. Let us mention first those two items you first mentioned, engineering expense Sarnia, of $17,000.00 plus, and technical and research expense at Sarnia of $2000.00 plus. Those two items are included under other expenses on Exhibit "304" and make up part of the $65,000.00 shown under other expense, Schedule 3, of Exhibit "280". Those two items represent engineering expense and technical and research expense within the Imperial Oil Company and represent the maintenance of Research and Development and Engineering Expense at Sarnia, which benefits all of the refineries of the Imperial Oil Company. The $27,105.00 which you mentioned subsequent to that under Engineering Development, appears as a separate item in Schedule 3 of Exhibit "280" as $27,105.00 under the head of Engineering Development. That is an item which is paid to the Standard Oil Development Company for fundamental development and research particulars, developing new processes and new methods of cracking and hydrogenation and catalytic operations and so on. So that the Imperial Oil Company will have available to it all of these new processes as they are developed and will not have to go out and pay a royalty for the use of those new processes when and as they are developed.

Q I was going to ask you now, if that is correct, Dr. Brown, that this Company is paying the Standard Oil $27,000.00 plus for all their new developments, why

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should they have to pay $20,000.00 plus on top of that to the Imperial before they get the Standard Oil information?

A I think these two things are entirely separate. Let me see if I can make that clear. The Standard Oil Development Company really operates a fundamental research and long time development, such as hydrogenation and catalytic cracking and alkalination and all of these new terms which you hear, and as these new processes become developed so that they are practical, it means that the Imperial Oil Company will have the right to use those processes without paying a royalty. That is the $27,000.00. Now in addition to that the successful operation of Turner Valley crude, for exanple, required a special treating operation. It has a lot of mercaptan sulphur in that crude which is difficult to remove by ordinary methods, and as I understand it, correct me if I am wrong, at Sarnia a new process was developed in which they could treat the gasoline by alumination and convert this mercaptan sulphur into hydrogen sulphide so that the sulphur could be removed by an ordinary alkali wash. That is a development that was worth a great deal to the Imperial Refinery at Calgary in cutting down their operating costs of Turner Valley crude. This was a problem which was not to be solved by the Standard Oil Development Company because it was a specific problem that had to be met by the Imperial Company and particularly at Calgary. It was solved mainly by the efforts of the Research and Engineering Department at Sarnia. Work of that kind would cover that $17,000.00

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and $2000.00 listed as engineering expense and technical and research expense at Sarnia.

MR. McGRATH: That is correct.

Q MR. COMMISSIONER LIPSETT: Then we come down to the first item on 304 which was Engineers. You said that it was right to have that extra number of engineers here in Calgary?

A Yes.

Q As I gathered, for what reason?

A Now, suppose that a pump breaks down at Calgary. I imagine that to get spare parts for that you would probably have to telegraph a few thousand miles and either wait for the railway or aeroplane to bring in the parts. That would require special shop facilities and special mechanical maintenance to be able to repair that pump so that they could keep the plant running. They have a lot of electrical equipment, and hydrometers and special measuring devices, and where it is possible to get repair parts promptly if we were in one of the large industrial centres, but not out here. In order to compensate for that they have to have skilled mechanics in greater number and of greater skill, perhaps, than would be necessary in the large centres.

Q To do that particular work without sending for the parts?

A Yes. In other words, they have to meet more emergencies here in a successful way than would be necessary if the plant were in the Chicago district for example. Then the other item about which you asked me which appears on Exhibit "306".

Q Technical services?

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A Technical services. That is something entirely different. Technical service, $11,397.00 on Exhibit "306" is a service of technical men who go out into the field to eliminate and explain these special difficulties which come up in the use of the products from the refinery. Suppose that some farmer out here who has a large acreage and a number of tractors found that the gasoline or the tractor distillate he is using caused his valves to stick, or caused some trouble with his tractors, he is going to assume that is due to faulty gasoline. In order that he keeps on using Imperial gasoline that difficulty has to be eliminated. That cannot be done by just the ordinary salesman or one of the agents of the Company. It requires special knowledge of some really expert experienced engineer. So that this engineer then goes into the field and finds out what the trouble really is with these tractors and remedies that difficulty and keeps that market, and selling his product. He has to do that because if that is not done the jobber handling the product will switch to some other product because of the complaints received by the jobber from this man using the tractors So that this $11,000.00 is more in the nature of what I early classified as a sales expense. All these services have to be made and perhaps in a small refinery you might find them all grouped together under technical or engineering division. Here they are subdivided into different types of service. Have I made that clear?

Q Yes, I quite follow that, Dr. Brown. I do not know

but that you might elucidate it a little bit further. Perhaps it is some difficulty in the tractor.

A Yes.

Q And the jobber switching to some other gasoline, he won't get any better results?

A That is right. But in the meantime the Imperial has lost that market, because the jobber has switched.

Q MR. FRAWLEY: That very question is the only thing that brought anything to my mind. You speak about these jobbers switching as though that was something which certainly you had had experience with in the United States?

A That is right.

Q I think that perhaps it would be only fair for you to study a little more closely the jobbers' operations here and the manner in which they are contracted to the Imperial Oil.

A You mean the jobber has no other source?

Q I mean, just to discuss it, the only other person to whom he could go, no question about that, is the B.A., Oil Company.

A All right.

Q They have certain jobbers. They have two large jobbers. But they might, I quite agree theoretically you are quite right, but all I was worrying about was the difference between theory and practice.

A Let us leave the jobber out. Suppose there is no jobber. Suppose it is a large farmer who simply comes to town and buys a couple of truck loads of gasoline.

Q From the Imperial marketing department. Well I can

[illegible]

see your point there. Suppose he is a man who purchases from the Imperial marketing department, he might switch as a consumer straight out of the Imperial and go into the offices of the Texas or the B.A.?

A Yes.

MR. COMMISSIONER LIPSETT: It is only fair to consider in that connection that if he had switched into the B.A., until recently, it was still Imperial gasoline?

A He would not know that. I think alot of these difficulties that are encountered in engine operation and laid to the gasoline, are due to some faulty operation of the engine. But it is part of the service to remedy that difficulty on the part of the user. If that is not done he will take another brand of gasoline. It may come out of exactly the same tank and he might not know the difference, but due to changed operating conditions he might get along for a while all right. It is one of those things that is in many ways intangible but it has to be met. There has to be a certain amount of service given to the user of these petroleum products. If that service is not given, the refiner who does not give that service will lose his market in time, or have a lot of complaints. And that giving of service has always been considered part of the load that should be carried by the refinery and that the marketing expense is simply selling the gasoline, making the contracts, and delivering it, but not servicing equipment in which it is used.

Q If there was a complaint about a product that that should

be referred back to the refinery?

A Yes.

Q And dealt with by them?

A If any one of us is a marketer of some product, and we get a complaint on that product, we do not try to explain it. We go to the man who made that product for us to sell and say "Here, you made this product. It is up to you to straighten this out." The Sales Department really cannot straighten out these technical difficulties. Another reason is that there might be something wrong with the gasoline. If so, this is the way the refiner learns about it so he can improve his treating process and produce a product which is more satisfactory. So by a matter of experience over many years these technical services are always in the producing department or the manufacturing department.

Q MR. FRAWLEY: Yes. Now that brings us to Exhibit.....

A That was "306." The next one is "307" which is a corresponding statement of General and Administration for Marketing, which is applicable to the Province of Alberta. Since we are not discussing marketing, we will pass that up. Now, "308" consists of three pages. First, an analysis of the products made and sold by the refiner. Referring now to "308-A" which is the first page, under the heading Refinery Production, we find in the first column the gallons of each product sold.

Q Dr. Brown, this is, of course, I think very vital that this Exhibit which is very important should be

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very fully explained. Is there any relationship between Sheets 1, 2 and 3? In other words, A. B. and C., does one lead into the other?

A Yes, I think these three sheets should be considered as one exhibit, as has been indicated by their numbers, "308", A., B., and C. The first sheet, or "308-A" is an analysis of the quantities of the various products produced by the refinery, and the second sheet is an analysis of the income and the amounts received per gallon for the various products, and the third sheet, "308-C" is an analysis of what might be called the Refinery Spread and Refinery Cost based on the operation of 1938, as it was during the latter part of the year from about June 20th, or so, on through December 1938. I am going back to "308-A" the first page of this group. The first column gives the sales in Imperial gallons, The amount of gasoline sold, however, is less than the amount of the gasoline produced by the refinery because of losses incurred in the selling and marketing end. So that 47,000,000 gallons of gasoline sold should be increased by 363,000 gallons representing losses incurred in marketing and handling the gasoline from the refinery to the marketing point. And should be further increased by 8,000,000 gallons that represented the amount of gasoline in the inventory at the end of the year 1938, or as of January 1, 1939. So that the amount sold, 47,126,000 plus 363,000, plus 8,627,000 and minus 13,000,000 representing the amount of gasoline in the tanks at the Refinery on January 1, 1938, represents the actual production of the gasoline during the year 1938 from January 1 to January 1, 1939,

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which is shown in the last column, 42,745,113 gallons. In other words, the last column on Exhibit "508-A" shows the actual production in Imperial gallons or Imperial gallons equivalent of each one of these products shown on the sheet after taking into account the marketing losses, the inventory of January 1,1938, and the inventory of January 1, 1939. Now there is one other item there under Bunkers, which is the fifth item. This refers to the heavy fuel oil which is left as a residue from the refinery operation. In addition to adjusting for inventories there, it shows another item in the next to the last column which is "Less Fuel from Processing B.A., crude." The Imperial Refinery processed about three-quarters of a million barrels of British American crude on a contractual relationship, which had a deduction of 9% of the crude as Bunker C fuel oil to be equivalent to the fuel used in processing the British American crude. And the cost of processing the British American crude and the service charge made by the Imperial Oil Company was based upon the crude without including the cost of the fuel, because the 1,516,940 gallons of Bunker fuel oil was given to the Imperial from the British American crude to compensate the Imperial for the fuel used in processing British American crude. It is a kind of complicated thing to explain but I hope that the record is clear. So we have 1,516,940 gallons of Bunker C which is subtracted from the Bunker Fuel Oil sold and in the inventories in order to find the Bunker fuel oil that was produced from the Imperial Company's crude oil.

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And the last column again, 7,707,246 gallons of Bunker fuel oil represents the net gallons of Bunker fuel oil obtained from the Imperial crude oil as processed at the Imperial Refinery while 1,516,940 represents the Bunker fuel oil from the British American crude which was retained by the Imperial Oil Company to reimburse them for the fuel used in processing British American crude. And the same statement or an equivalent statement applies to the refinery consumption of fuel, which is the next item. Again there is 637,450 gallons equivalent of gas and fuel which was consumed in processing the British American crude and obtained from the British American crude. So that the last column under Refinery Consumption, 1,888,011 gallons represented the gallons of oil equivalent to the refinery gas used in the refinery as fuel for processing Imperial's crude. So that the summary at the bottom of Exhibit "308-A", rather the last column of Exhibit "308-A", shows the actual production of all these products from Imperial crude and the Casing Head gasoline and crude naphtha which were run by the Imperial Refinery for their own account during the year 1938, 70,407,571 gallons shows as the sum of all these items, and checks with the 70,407,571 shown at the bottom of the Exhibit "308-A" as representing the total amount of material brought into the Imperial Refinery and run for their own account.

Q Exhibit "308-A" then is an effort to show just what various kind of products, as listed here, the Imperial got out of the crude oil and the other refining material

which they put into their refinery in 1938, on their own account?

A On their own account.

Q On their own account?

A After making all deductions and corrections for the British American crude which was processed for the British American.

Q In other words they got 70,407,571 gallons of gasoline, refined oils, tractor distillate, light fuel oils, bunkers, refinery consumption, asphalt, coke and unfinished stocks and loss?

A Yes.

Q They got that out of the total crude, separator naphtha and absorption gasoline that they fed into their refinery in the year 1938?

A For their own account?

Q And blending stocks?

A Yes.

Q For their own account?

A Yes, that is right.

Q MR. COMMISSIONER LIPSETT: That is the figure that we get in Schedule 3 of Exhibit "280" as amended to 2,753,587?

A No.

Q Having taken off that.....

A I think I can explain that. McGrath, you check me. 2,753,587 barrels on Schedule 3 of Exhibit "280" is the same as the 69,032,397 gallons shown on Exhibit "308-A" which does not include the blending stock of 1,375,174 gallons. In other words, it is the upper figure.

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Q It corresponds with that 69,032,397?

A I think that is correct.

MR. McGRATH: That is right. The 2,753,000 includes.....

A No, that is not right.

MR. McGRATH: Includes British American crude?

A That is not right. It includes....let me correct that for the record. The barrels shown on Schedule 3 of Exhibit "280" as 2,753,587 are the number of barrels which include the 69,032,397 gallons of crude, absorption and crude naphtha, which were run by the Imperial for their own account, and in addition the 781,233 barrels of British American crude run for the British American Company.

MR. McGRATH: That is right.

MR. COMMISSIONER LIPSETT: By deducting the British American in barrels from this 2,753,587 then I should get this 69,000,000 odd in gallons?

A That is correct.

(At this stage the Hearing was adjourned until 10.30 A.M., 15th June, 1939).

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The Province of Alberta

IN THE MATTER OF THE PUBLIC INQUIRIES ACT

—and—

IN THE MATTER OF a Commission, dated the 12th day of October, A.D. 1938, to inquire into matters connected with Petroleum and Petroleum Products

Commissioners:

The Honourable MR. JUSTICE McGILLIVRAY
(*Chairman*)

—and—

L. R. LIPSETT, ESQ.

Session:

CALGARY, Alberta June 15th, 1939

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DR. G. G. BROWN, having been recalled, continued examination by Mr. Frawley:

Q MR. FRAWLEY: Dr. Brown, before we proceed to further put into the record a description of Exhibit "303", I want to discuss with you what took place yesterday with regard to the question of obtaining an estimate of the British American cost, the Mayland Company's cost at the new plant, and the Lion Company's cost at the new plant, and particularly with respect to what was said or left unsaid at that time with regard to the proposed Imperial plant. I take it that you do not know very much about the new Imperial plant?

A Practically nothing.

Q And that applies to all of us. Now if I put it to you that there was a newspaper announcement by the Company that they intended to construct either a new plant or to construct new some part of the present, reconstruct new, some part of the present plant, as I understand, to materially affect their operations here, if that were said and then assuming further that at the moment there is no part of that construction yet begun, now would you compare that situation, which is a very meagre description of it, I admit, compare that situation with what is in fact at the British American plant, if you will assume with me that the fires were first put under the stills on the 26th or so of April of this year, in your opinion as an expert in these matters and a chemical engineer, is there any difficulty between your ability to go out and obtain useful information for the Commission at the British American plant and go out and obtain useful information with respect to the new Imperial operations when its plant has been built?

A Well, my attitude is that there is a sharp line of demarcation between what may be regarded as history, such as we have been discussing in these Exhibits, which represent the result of an operation which has been completed, for the year 1938 on one hand.........

Q Yes?

A And on the other hand, in estimating on future operations which have not yet been completed, and I think that line should be made very distinctive; in other words, the operations which have been completed in 1938 are behind us, and it is a matter for an accountant to ascertain and figure out what has been done. The operations on the British American refinery, which has really not yet been connected on the stream or any other operation which has not yet been completed, must, by the very nature of the thing, be an estimate.

Q Yes?

A Now of course it is more easy to make a reliable estimate of a plant which is just beginning to operate, than it is of a plant which exists as yet only on paper, but I feel that they would nevertheless both be estimates.

Q Yes, both be estimates of comparable value?

A Well yes, an estimate is an estimate and if they are done with equal care they are probably equally reliable.

Q Now, let me put it to you, the Commission is commissioned to ascertain the fair and equitable cost, at this stage of this Inquiry, the fair and equitable cost of refining gasoline or petroleum products in Alberta, and unless the one with respect to which we have the history, the only one of which we have the history, unless it is typical, it is as good as the most efficient, for instance, then there is some question, is there not, as to the advisability of the Commission accepting without any further inquiry

[illegible]

... [illegible] a long line of
[illegible] that may be regarded as history,
such as [illegible] in these Exhibits, which
[illegible] which was [illegible]
completed, [illegible] the [illegible] hand...... [illegible]

Yes?

And on [illegible] on [illegible]
which have not [illegible], and I [illegible]
[illegible] very difficult [illegible] in other [illegible]
[illegible] rations which [illegible]
[illegible] it is [illegible] that [illegible] to ascertain and
figure out [illegible] the [illegible] of the
British American [illegible] has really [illegible]
[illegible] of the [illegible] operation which [illegible] not
been completed, [illegible] the very nature of [illegible]
estimate.

Yes?

Now of course it is [illegible] make a reliable estimate
of a plant which [illegible] going to operate, than [illegible]
of a plant which exists [illegible] only on paper, but [illegible]
that they would nevertheless both be estimates.

Yes, both [illegible] estimates of comparable value?

Well yes, an estimate is [illegible] estimate and if they are [illegible]
with equal care they are probably equally reliable.

Now, let me put it to you, the Commission is endeavouring
to ascertain the fair and equitable cost, at this stage of
this inquiry, the fair and equitable cost of [illegible]
gasoline [illegible] petroleum products in Alberta, and unless
one wishes to refer to [illegible] have the history, the [illegible]
one of which [illegible] history, unless it is [illegible]
it is as [illegible] efficient, for instance, [illegible]
[illegible] is [illegible] there not, [illegible] to the advisa[illegible]
[illegible] without [illegible] inquir[illegible]

G. G. Brown

the purely historical picture as presented through the Imperial's experience in 1938, is there, or is there not, in your opinion?

A Now that is a hard question, the way you put it, because you have an "unless", whatever phrasing you used, unless the past operation which is now history is typical or is... ....

Q Efficient?

A Most efficient.

Q Yes, is the most efficient?

A Yes, unless that is true........

Q Unless that is true, then is there not some danger in the Commission limiting itself entirely to an examination of that picture?

A Well, it is not for me to say whether or not the examination should be limited to that picture. If I can break down your question.........

Q Yes, break it down?

A Into two parts.

Q Yes?

A I might give an answer which might be of more value.

Q Yes, do that?

A First of all, I believe that the operation as presented in these Exhibits of the Imperial plant as representing the operation as extending during the last six months of 1938, where they had high throughput, the plant was operating up to capacity, is really a very efficient operation as far as costs go, and I doubt if an analysis or an estimate of any other operation which is now contemplated will show costs that are below that.

G. G. Brown

Q Yes.

A Yes, now if we can dispose of that as one item?

Q That is a big step forward?

A Then the other question you asked me is whether or not it would be advisable to limit the consideration only to that plant.

Q Yes?

A Due to the answer I have just given you that I believe that operation will show as low a cost as any operation that has been contemplated and disclosed to me, I believe that the Commission would be safe in taking that as a low cost operation.

Q Yes?

A However, they perhaps would want to become more certain in their own minds whether or not my opinion is correct, that that is a low cost operation.

Q And how would they go about arriving at that feeling of security?

A That would be by a comparison of the estimates of other operations, either to be built as now contemplated, or as the Chairman put to me the other day, a hypothetical operation based on some reasonable assumption.

Q Yes, so if you were being asked to, let me put it this way, if you were being asked to advise the Commission as to what directions they should give, or to advise me, is perhaps the better way to put it, what steps I should take, you feel you should be free, you or anyone else retained, to examine fully into the British American plant, physically as it now stands, and any figures of capital investment which they might prepare and submit to you and any figures of operating costs which they might prepare, and submit to you.

G. G. Brown

A On the plant as it now stands.

Q On the plant as it now stands?

A Well that has been done.

Q The British American?

A I beg your pardon, I thought you said "Imperial".

Q No, if I did, I meant the British American, you think I should make every effort to have made available to you the physical plant itself of the British American Company, any capital costs which you can ascertain from the company to check against any capital costs which you might estimate yourself from looking at the plant?

A Yes.

Q And any figures of operating costs which they might have to submit to you to check against what you might estimate to be the operating costs of the plant?

A Yes, I think all such information will be very helpful in a thorough exploration of the situation, so that the Commission will have entire confidence in the opinions and recommendations which I might make.

Q From this historical experience and from the actual experience?

Q THE CHAIRMAN: Of the Imperial?

A Well..........

Q MR. FRAWLEY: Now wait, let me follow you?

A I was speaking in generalities.

A Any information of plants now constructed and going on stream, or plants to be constructed in the future of which we have some knowledge.

Q Yes?

A Will of course make the investigation more thorough, and to

G. G. Brown

that extent would probably place more confidence in the conclusions obtained.

Q Yes, I know, but when you speak of conclusions obtained, you are speaking primarily of the actual cost for the year 1938 of the Imperial plant, which we have put in as the Exhibit?

A No, let me elaborate that again, as I recall yesterday the Chairman clarified the situation by asking me to take the point of view of advising some large purchaser of fuel as to what would be a fair price he might expect to pay.

Q Yes?

A During the coming year or the coming two years based on conditions as they now exist and as they probably will exist in the next year or two.

Q Yes?

A Now, that of course is an engineering estimate and requires the use or the drawing of conclusions based upon opinion, and the more information one has to substantiate his opinion or to use for a basis of his conclusions, usually the more confidence there is in the accuracy of those conclusions,

Q Yes, but as I understand, Dr. Brown, when the Chairman put that to you yesterday, you said you would, before giving an opinion of this hypothetical kind, that you would examine into all the operations of the people who would be likely in the field to supply that contract?

A That is correct.

Q And therefore you would want to bring, bringing you right down to Calgary, you would want to look at the Imperial plant, the British American plant, the proposed Imperial plant, the Lion plant, and the Gas and Oil Products plant?

G. G. Brown

A	Yes, and any other plants which might be proposed or seem likely to be constructed in the immediate future.

Q	Yes. Now I think I understand that to this point, and you have told me what you think you should be allowed to do, and that you could usefully do in connection with the British American plant. Now then what do you suggest that you could usefully do with regard to the proposed Imperial plant?

A	If the Imperial Oil sees fit to give me the benefit of their estimates and their information, I will have a better basis to estimate the probable cost and efficiency of their new plant as it will be in existence in a few months; otherwise, all I have to go on is what you have told me appeared in the paper.

Q	Then assuming that the Imperial will give you all that information, then you would be able to use that in comparing that or putting that down beside the information which emerges from the Exhibits which Mr. McGrath has filed?

A	That is correct, and the same statement would apply to the British American or any other similar operations.

Q	Then we come to the Mayland plant which I am informed yesterday has only reached the stage of the concrete foundation being erected for the cracking unit, but nevertheless you feel if you went there and discussed the situation thoroughly with the officials involved and went into the question of the capital cost of this plant, of the proposed operation, that you could in that instance again, come to the Commission with a useful estimate as to what that company is prepared to produce petroleum products for?

G. G. Brown

A I understood that was the proposition or problem which was put up to me, and that is the way.....

Q That is the way we left it yesterday?

A And that is the way I would go at it.

Q And then also to complete it, also with respect to the operation of the Lion Company in Calgary?

A Yes.

Q Now, Mr. Chairman, that certainly clears it, and I think the discussion we had yesterday, Mr. Nolan did not think that it had been suggested to his company to make this kind of information available to Dr. Brown, and lest there be any misunderstanding at all either on the part of Mr. Nolan or the other companies, I think it should be made very clear, and I should now say to Mr. Nolan, in view of Dr. Brown's statement, as I have said to Mr. Harvey, and indeed I have made some progress with Mr. Harvey, that the information which Dr. Brown has now intimated he would like, I would like that to be made available to him, either here or in Toronto or at Ann Harbor at the earliest possible moment?

MR. NOLAN: It is not quite enough to say "Mr. Nolan did not think", the fact was we were not asked for it.

MR. FRAWLEY: I read the record this morning and I cannot disagree.

MR. NOLAN: I do not mean only on the record but at no time during these proceedings.

MR. FRAWLEY: Oh no.

MR. NOLAN: We were asked to prepare what was our experience in manufacturing costs, and to the best of our ability we have done that. This is new.

MR. FRAWLEY: Oh, it was new from yesterday, certainly.

THE CHAIRMAN: This body is probably responsible for that, Mr. Nolan, and we were just thinking of things as we go along. I take it there will be no difficulty making available to the witness the information which he thinks would be helpful to him.

MR. NOLAN: I have not had an opportunity to discuss this matter with my client, but I do not think so.

MR. FRAWLEY: I think all we can do is to ask Mr. Nolan.

MR. NOLAN: Up to the present, they have been very helpful.

MR. FRAWLEY: Oh yes.

MR. NOLAN: At every stage.

MR. FRAWLEY: Oh yes.

THE CHAIRMAN: From the standpoint of your company, Mr. Harvey, I presume you see no difficulties in the way?

MR. HARVEY: I think they will co-operate in anything of that kind.

THE CHAIRMAN: Yes, I feel quite sure they will, and you do not anticipate any difficulties in any examination Dr. Brown wishes to make, that will be made possible through the co-operation of your client, Mr. Shaw.

MR. SHAW: No, I do not anticipate any. I have not spoken to my client about it, but I will be very glad to do it.

THE CHAIRMAN: Oh, I think from the spirit in which this Inquiry has proceeded thus far that you

need not anticipate any difficulty from any responsible company in giving us or any expert witness you may call, any information which he thinks may be desirable.

MR. FRAWLEY: No.

THE CHAIRMAN: That has not been anybody's attitude, and I am quite sure it will not be.

MR. FRAWLEY: No, I am trusting it will not be, and I do not think it will be.

Q MR. FRAWLEY: Now, Dr. Brown, will you complete your discussion of the Exhibit "308"; we had just reached the very vital part of it yesterday afternoon, and we had only completed the first page, Page 308 (A)?

A I think I have this matter straight, we were just discussing the balancing of the ,of referring to "308" (A), which I think was the last one, I think the last statement which was made was the 69,032,397 gallons, shown as the total quantity of crude oil, absorption naphtha, and crude naphtha processed for the Imperial Oil Company when converted into barrels, amounted to 1,972,354 barrels, and that the total amount of crude oil, crude naphtha, and absorption naphtha that was processed by the refinery is then obtained by adding to that figure, 1,972,354 barrels, the 781,233 barrels processed for the account of the British American Oil Company, and that the sum of those two figures equals the 2,753,587 barrels shown in the first line of Schedule 3, on Exhibit "280". I believe that was your last question, so that that really completes the explanation of Exhibit "308" (A).

Now, referring to the Exhibit "308" (B), this is a statement of the gross income less freight received by the Imperial Oil Company

[illegible] not [illegible]

[illegible] in giving [illegible]

[illegible] information [illegible]

[illegible]

[illegible] discussion of the exhibit [illegible]

[illegible]

only completed [illegible]

I think I have this [illegible]

[illegible] 30,000,000 [illegible]

[illegible]

for the products sold for their own account. On the left-hand side of the sheet are those that were sold through their own marketing organization , and on the right-hand side are those products that were sold through jobbers, the total sales under gasoline.........

Q If you take the gasoline purchased and explain that thoroughly, then the rest follows on, would they not then be self-explanatory?

A I think so.

Q Yes?

A The gasoline here includes all of the brands of gasoline sold and the sales have been totalled, both as to gallons and to amounts. The item plus freight which is added in as the second item under the return for the gasoline is added in for the reason that the total sales as reported in the first line do not include the item of freight which has been taken out of the total sales, and put in a separate freight account as I understand it, and that freight on the Ioco naphtha should be added in as part of the additional receipts because that item was previously subtracted from the receipts and put into the freight account, so that to the amount shown as received for the total sales of gasoline, is added an amount equal to the freight which was paid on the Ioco naphtha.

Q And solvent oil?

A And the solvent oil, the other blending stock. Then some gasoline was sold through their own marketing organization from Coutts. That is subtracted from the gasoline sold, the total.

Q From the Coutts refinery?

A From the Coutts refinery. In order to arrive at the quantity of gasoline and the amount received for that

G. G. Brown

gasoline which was sold from the Calgary refinery.

Q Yes?

A You will note that apparently no such sales were made to jobbers but were made only to their own marketing organization; in addition to that, at various times, apparently purchases of gasoline were made and in turn sold to their marketing organization and also to their jobbers, so that these outside purchases should be also subtracted from the total amount of gallons and also from the total amount received in order to arrive at a figure representing the quantity of gasoline sold from the Calgary refinery and the dollars received for that gasoline.

Now, in the present analysis the sales made to the marketing organization are priced on a different basis than the sales made to jobbers, and the only accurate or reliable way to estimate or to determine rather the value of the products made by the refinery is to determine what price was received for those products when sold to the jobbers or some other purchaser, not simply another division of their own company, so for that reason the left-hand side of the sheet, Exhibit "303" (B) may be neglected insofar as any further discussion is concerned, and we can confine our attention to the quantity and the amount under the column headed "Jobbers", because the selling of the product of the refinery to jobbers is the only satisfactory way of determining the market value, and therefore the actual value of the product produced by the refiner.

Q At the refinery?

A At the refinery.

G. G. Brown

Q Now the 13.39¢ though, where does that figure come from, that is the price per gallon for the sale to the marketing organization, now where does that figure come from, it is shown as the price, as the per gallon figure of the total sales to the marketing organization?

A I understand that corresponds to the tank-wagon price.

MR. MCGRATH: That is right.

MR. FRAWLEY: If we know it is not sales to the marketing organization?

MR. MCGRATH: It is not.

WITNESS: It is a sale by the company, sales made by the company through its marketing organization.

MR. MCGRATH: That is right.

MR. FRAWLEY: But it is intended to represent the refinery price.

MR. MCGRATH: No, no.

WITNESS: No, no.

MR. MCGRATH: The marketing expense has not been deducted from that, Mr.Frawley, that is just, it shows at the top, the gross income less the freight, sales tax and packages, but there are no marketing expenses in there. It is a realization by the Marketing Department.

A In other words the marketing department is part of the Imperial Oil Company and the 13.89 cents represents the amount received by the Company through its marketing organization by sales made through the marketing organization. That does not represent the value of the gasoline at the refinery but rather at some other point in the province and is really the net tank waggon price.

Q MR. FRAWLEY: I think I understand it. But let me ask you this. I am a little bothered as to why it is in this Exhibit?

A Well this Exhibit "308" (b) as I understand it is a complete report of the sales and gross income, less freight, as received by the Company.

Q Yes, I am only asking these questions to understand. I am not critical. But this Exhibit "308" (a), (b) and (c) is to lead to a determination of the company's refinery profit?

A That is what I am using it for. It may be also used for other purposes. This same information may be used in determining the profit of the marketing division.

Q But you put it a moment ago that we could disregard the information contained on the left hand side of the sheet Exhibit "308" (b) for our further consideration of the refinery profit?

A That is right because the value or the market price of the material produced by the refinery must be determined by what some outsider is willing to pay and did pay for that material at the refinery.

Q You are arbitrarily regarding the marketing organization as though the head of that organization, Mr. Halverson, were a

jobber and purchasing at the refinery door his requirements from the refining department?

A In other words we are trying to make the marketing department stand on its own feet.

Q For the purposes of arriving at the refinery spread as distinguished from the marketing spread which we will discuss later?

A We have a refinery spread or increase in the value of the crude and other material as it passes through the refinery. In other words, the refinery spread is the number of dollars received for the products from one barrel of crude oil at the refinery minus the cost of that barrel of crude oil at the refinery.

Q Yes, let me put this to you as to whether it is the proper definition of spread insofar as we have any interest in it in this refinery in this province. It is the difference between the cost of the refining material and the realizations from the jobber by the refinery on finished products?

A The difference between.

Q Between the cost of the refining materials?

A Refining?

Q Refining materials. Crude oil.

THE CHAIRMAN: Are you saying the refining of materials or the cost of refining materials?

MR. FRAWLEY: No, that is an adjective. Refining materials, the crude oil.

A All right.

Q The difference between the cost of refining materials?

A You mean raw materials.

Q Yes?

A Such as crude, naphtha and absorption.

Q Right. And the realizations from the jobbers at the refinery, all realizations on finished products from the jobbers at the refinery?

A Yes. That term "refining materials" is rather confusing.

Q What should that be Dr. Brown?

A I would say crude oil, naphtha and absorption.

Q Yes, I see. The difference between the cost of crude oil. Yes?

A And naphtha and absorption. That defines it well enough.

Q On the one hand and the realizations on the finished products at the refinery from jobbers?

A That is right.

Q Again treating the marketing department as a jobber. Oh, I doubt now whether that helps.

A The marketing department has to be divorced from the refinery on some basis in order to make an indpendent study of the refinery. It seems that the only logical way to do that is to divorce it entirely and assume that the refinery received for its finished products a price that it received from the jobbers at the refinery door.

Q I think perhaps that does not help for me to say ---- well I will just leave it as jobbers. Realizations on finished products from the jobbers at the refinery. In other words what you call the refinery spread is the difference between X cents, which is the cost of crude oil and naphtha and absorption going into the refinery at the entrance door and what it gets from a jobber or

all the jobbers combined at the exit door of the refinery?

A That is right.

THE CHAIRMAN: All that we are saying presupposes the necessity for there being jobbers, which, I suppose, will at some time be discussed?

MR. FRAWLEY: In the marketing discussion, Oh yes.

THE CHAIRMAN: All right.

A I think I understand your statement. I do not want you to feel that this price that we are arriving at is a price which would be different if there were not jobbers.

Q Yes, I see.

A It is a price or value received for the finished prodcuts at the refinery. It is impossible to arrive at that from the marketing organization of the Imperial Oil Company itself unless we know how much cost there was and what profit there was in the marketing division of the Imperial Oil Company. Now the jobbers have to bear their own cost and their own profit, after paying a certain price at the refinery. And it seems that is the fair value to put on the products as produced by the refinery. Then if the marketing division of the Imperial Oil Company has been able to operate on less money than is represented by the difference between what the jobber paid and what the marketing department sold the products for, then the marketing department is making money and the profit made by the marketing department should be charged against, or credited to the marketing department and not to the refinery.

Q Yes. What we are momentarily concerned to arrive at

then, is the price paid by anyone whether called a jobber or not?

A That is right.

Q At the exit door of the refinery?

A That is right.

Q And that is arrived at, I take it, by determining what, so well as one can, what the product has cost to create from the crude article, making an allowance for such proper profit in respect of the operations there might be. I mean knowing what is sold to the jobbers for alone does not matter, does it? It may be sold to them too high or too low?

A What you have stated would be the way a price controlling commission might look at any operation operating more or less as a public utility. But what I have done here is the exact - or what is done here is the exact reverse of that. In other words, we are trying to find out how much the company made from their operation at the refinery.

Q And see is that a fair return?

A And come back and see whether that is a fair return or not. It is getting to the same answer but travelling the road in the opposite direction. It seems it is about the only way we have of going at it. Because we know what we have paid for the crude and the naphtha and the absorption and by this Exhibit "308" (b) we can determine how much they received for the products sold at the gate of the refinery.

Q You say if the jobber or anyone standing in his shoes was charged too much that would be reflected in what were seemingly excess profits?

A That is right.

Q By the method by which you approach it?

A Yes.

Q At least by the method by which it has been approached and into which you are asked to examine?

A That is correct.

Q MR. FRAWLEY: In commencing a study of these costs, I understand you found there was really no such thing as a refinery tank car price, for your purposes?

A Yes, that statement is correct. That price is based upon a tank waggon price less certain discounts and with some freight and taxes involved in there.

Q But I mean to say, that is not just quite what I meant. In the United States there is a well known quoted posted tank car price at the refinery?

A In some areas.

Q In some areas at which any person can go and buy?

A That is right.

Q Did you find there was any departure from that situation when you began a study of this Imperial situation at Calgary?

A No, I have not investigated that thoroughly but it is my information that practically no gasoline is sold that way in Calgary.

Q Yes?

A We find that same condition in parts of the United States also. That all of the gasoline which is sold is sold either through regular jobber contracts or through their own marketing organization.

Q Now is that why then you take these jobber contracts

and made them, as you might say, the posted tank car price at the refinery for your purposes of determining the refinery spread?

A Yes, that is correct, that there is no posted price at the refinery at which jobbers and other people can buy.

Q And so for your purposes you take, you regarded the marketing department - you divorced the marketing department from the refining department itself for the purposes of arriving at the true refining spread as distinguished from the true marketing spread?

A Yes.

Q And that is why you have laid emphasis on this jobber price. That to you is the effective tank car price at the Calgary refinery?

A Yes. If I understand you, yes.

Q I think this should be cleared up now. I hope it is not getting too much into marketing. If I do not go beyond Exhibit "257", which is a sheet of posted prices generally, and if I merely put this information to you which you will have to assume with me, Dr. Brown, as correct until it is put into the record as evidence, if you assume with me the posted tank car price on Esso?

A Tank car?

Q Tank car price on Esso and Three Star gasoline is 1½ cents under the posted tank waggon you would immediately reject that as the effective refinery door price?

A Unless practically all of the refinery products were sold on that basis.

Q That is true. But if there were added to that that practically no part of the product is sold on that basis then you would pay no further attention to that?

[illegible]

A That would have no significance in determining the refinery price.

Q And if I put it to you that was the posted tank car price of these two gasolines, then I presume you would say there is no tank car price as far as that goes?

A That is right.

Q And if I put it to you that the Company for what it calls its Renown ~~Fuel~~ and Renown Gasoline, which is a brand which they sell to certain jobbers - if you take it from me that is so - the tank car price on that is $3\frac{1}{2}$ cents under the posted tank waggon price of Esso and Three Star, would you again say it was not as far as you were concerned the effective tank car price?

A Unless appreciable quantities were sold on that basis.

Q And if they were not appreciable, but if they were a minor part of the output sold on that basis would you again reject that and go to the contract jobber price and use that?

A I would take that into consideration, whatever minor factor it was. These prices have not been arrived at by any consideration of tank waggon price. These represent the averages per gallon on the dollars actually received by the company in 1938.

Q From jobbers?

A From the jobbers, yes.

Q Let me understand it?

A In other words, it is not taking the tank waggon price and taking any spread or any freight, because these spreads and these freight allowances may vary through different parts of the province. This is history, the

actual dollars received.

Q At the refinery?

A At the refinery from the jobbers.

Q Even though the method of quoting the price to the jobber under these contracts may be so much under the tank waggon at destination, that is a mere circumstance?

A Yes. To be specific, there may not have been a single gallon sold from the refinery at 8.96 cents indicated in the first line on Exhibit "308" (b) but in the aggregate all of the gasoline sold to the jobbers would have netted back under these conditions that 8.96 cents.

Q And as I said at the beginning, I am trying to be helpful of course but it may be that this does not help at all but only confuses us, I want to know why you have rejected that gallonage that is sold to certain jobbers 3½ cents under the tank waggon?

A I have not rejected it. I have rejected nothing. Everything has been included in here. If we were to take these various tank waggon prices and these various discounts and freight allowances, I would have to know exactly how much gasoline was sold on each one of these quotations.

Q MR. NOLAN: And this would be the answer?

A This would be the result and that would be a very difficult way to get at it.

Q MR. FRAWLEY: You say this is in there. Now perhaps I should clear this up. If Mr. McGrath can help me I wish he would. It may be that this Renown gasoline that I am putting to you is not sold by the Imperial at all but by one of its subsidiaries and that is perhaps why it is not in there at all?

A It would not make any difference, if it was sold and produced by this refinery at Calgary. If it was produced at the refinery at Calgary and sold to the jobber it is in here.

Q MR. FRAWLEY: Mr. McGrath, you could clear this up. I understand what you call Renown gasoline and is now being sold to the Gas & Oil Products at $3\frac{1}{2}$ cents under the posted tank waggon of Esso and Three Star?

A I do not know.

Q That is what Mr. Halverson told me. Where is that in there?

MR. MCGRATH: This is the average of all these sales. Whatever these prices are there.

Q $3\frac{1}{2}$ cents?

MR. MCGRATH: It is an average of all the sales made to jobbers.

Q 8.96 cents?

A MR. MCGRATH: 8.96 cents is the average of the whole business.

MR. FRAWLEY: Thank you very much.

DR. BROWN, recalled.

Q MR. FRAWLEY: Now then, how far had we got along on --

A I believe I had just finished stating that the gasoline bought by the Imperial Oil Company and not produced at the Calgary refinery and in turn sold through their own marketing division or to the jobbers is deducted both in quantity and in receipts. So that the last line under gasoline representing those totals shows on the left hand side the total quantity of gasoline sold by

the marketing division which was produced on the Calgary refinery. And the next line the total amount of money, in this case including freight on the Ioco naphtha which was received for that gasoline, and by dividing the last figure by the former we find an average of 14.13 cents per gallon as being the average received by the marketing division of the Company for the gasoline sold by the marketing division that was produced at Calgary. But because that includes marketing costs and marketing profits and other things that figure is not considered in arriving at the refinery return for the finished product sold at the gates of the refinery. The column at the right hand headed "Jobbers" shows 18,182,000 plus gallons of gasoline sold to jobbers as produced from the Imperial Refinery at Calgary and for that an amount equal to $1,655,000.00 was received. Which means on an average in the aggreggte 9.1 cents was received from each Imperial gallon sold from the Calgary refinery to jobbers and similar purchasers.

Q Yes. Now this is the average return at the refinery, sale price at the refinery, 9.1 cents for all gasoline, the three gasolines as you understand it and as I understand it?

A Yes, that is right, as sold at the refinery to jobbers and similar purchasers.

Q The importance of that is that that is the figure you are going to pursue along through to the end?

A That is then the value of the gasoline that was produced by the refinery.

Q Yes, and there is no account taken of the differential that is received at the refinery for Esso gasoline as distinguished from Acto or third structure gasoline?

A That is all in there.

Q That is all in there? It is just 18,000,000 gallons of all kinds of gasoline were sold and $1,655,000.00 was received from the jobbers for all that gasoline?

A That is right.

Q And simply one is divided into the other?

A That is right.

Q And in this statement there is no attempt made and as I understand it is impossible to show and would serve no purpose to try and show what these jobbers paid for Esso gasoline as distinguished from what they paid for -- or could that be done?

A There is no purpose in doing that if we are trying to arrive at the refinery spread.

Q The refinery spread?

A Because whatever the refinery sold it sold and whatever it received it received.

Q Whether it sold products (a), Esso at too much or too little as compared with Three Star and Acto, is of no importance to you as far as this study is concerned?

A No.

Q Whether it is that third structure gasoline is being sold too low in comparison with what price is being charged for the Three Star and Esso that is another way of saying the same thing, that is of no importance to you in making this study.

A That has not been considered at all in arriving at this refinery spread. That is really another question.

Q MR. COMMISSIONER LIPSETT: Would it not be important to get that figure broken up. Supposing the spread on

lower grade gasoline in which there is some competition in this province was too low and the spread on the higher types was too high, would it not be of importance for us and for you to consider? There are three grades I understand and so far we have heard there is competition in the lower grade. In fact it was suggested that the third structure gasoline was being sold too low at present prices. Don't you think it would be important for you to be able to consider that and get that figure broken up?

A For a different purpose, yes. That is if you are concerned with competitive conditions and what effect these competitive conditions might have on the different prices received for the different products, it is a very important consideration. To make my point clear. Let us suppose that there are some plants which are equipped only for producing third grade gasoline and a fuel oil. That may not be true but let us make that assumption for the sake of the discussion. If there are a number of those plants operating there will then be a large production of third grade gasoline and fuel oil and all of that material seeking a market will tend to decrease the price of third grade gasoline and fuel oil. So that the refiners who are equipped only for making third grade gasoline and fuel oil have no other opportunity for making any profit or making their expenses except from what they can get for third grade gasoline and fuel oil. If there was a reasonably good demand for extremely high quality aviation gasoline and only one refiner was in the position of producing this high quality aviation gasoline, he might be in a position to charge a sufficient price for this premium

[illegible] There are three [illegible]

[illegible] being [illegible]

[illegible] my point clear. [illegible]

[illegible] which [illegible]

[illegible] so that assume [illegible]

[illegible] There are [illegible]

[illegible] be a large fraction of the [illegible]

[illegible] and all of the [illegible]

[illegible] the price of [illegible]

[illegible] gasoline [illegible]

[illegible] quite [illegible]

[illegible] than [illegible]

[illegible] extremely high quality [illegible]

[illegible] in the position of [illegible]

[illegible] gasoline, he [illegible]

[illegible] this [illegible]

aviation gasoline to make a profit on that which might compensate him in such a degree that he could afford to continue selling the third grade gasoline and fuel oil at prices where the other refiner really could not make his expenses. I believe that is something that was in your mind perhaps?

Q Yes, there were two thoughts I would like to get your opinion on at some time. One is that particular question as to whether a competitor who only sells third structure is getting a fair price, or whether that present price, if too low, is forced on the Imperial Oil by reason of these other refineries that only produce third structure; or a third alternative, whether they do that with a view of exercising perhaps too much pressure, too much competition on these small competitors. Then as a second line of thought that one might like you to consider and that is if the sale price of third structure gas is the current price whether then the spread having regard to manufacturing costs is correct or if too high between that third structure and the standard and the Esso?

A Your question really can be answered in a satisfactory manner only on the basis of one assumption or another. In other words, we can assume that it is a condition of free competition in which case everybody charges what the traffic will bear and the consumer has as his protection only the competitive condition. Under such conditions then a fair price for the aviation premium gasoline might be very high and the money made on selling that high grade gasoline would compensate

[illegible]

[illegible] these [illegible]

[illegible]

for the low price received for the third structure, and the price received for the aviation gasoline as compared to the third structure would be entirely out of line, perhaps, in relation to their cost of production. But it would be a fair price based on the competitive conditions. Or we can take the opposite point of view --

Q Really in that particular instance it is a fair price based on the fact that there is a monopoly in the aviation gasoline, in your hypothetical case is it not?

A You mean --

Q In the case you gave us there is only one company manufacturing aviation gasoline and that would create a monopoly as far as the aviation gasoline is concerned?

A That is right and because the aviation gasoline is selling at a high price there is a large profit in it the assumption is that there will be immediately or very shortly brought into the field another producer of that product and then that price will come down. If we have more than one producer or manufacturer making all of the different products then we do have a state of competition. Now we can look at it from the opposite point of view, that is the capital, the cost of production and a reasonable return on the capital investment. In other words, regard it as a public utility. In that case if we have more than one refiner, and we have one refiner producing third structure and fuel oil only, we then would have to fix a price that would keep him in business getting a fair return and the price that would be fixed would be a price that would keep the highest cost producer in the field and

hen we have a higher price perhaps for third structure nd a lower price for aviation gasoline. Now the way t works out on paper in the ideal case is that if all he material, if all of the products required by the erritory to be serviced are produced by more than one ompany, we should find substantially the same price ue to that competition as would be arrived at under onditions of a public utility when the cost of production as been correctly determined and the prices fixed accord- ngly. That is the ideal solution to it. Now, of course, nder conditions of free competition where there is only ne company capable of producing all the products that ompany will have an advantage in those products in which here is no competition. So that if we have a competitive ondition in this territory on the various products of asoline and refined oil and tractor distillates and other roducts the free conditions of competition will strike a alance between the selling price of those various products, hich will not always be actually in line with what the ost of production will be, but there will be a balance o that in the aggregate there will be a reasonable return n the capital invested.

Q That is on the assumption of competition?

A That is right.

(At this stage the hearing was adjourned until 2:00 P. M.)

(EXAMINATION OF DR. BROWN CONTINUED BY MR. FRAWLEY)

Q MR. FRAWLEY: Now Dr. Brown, would you complete your discussion of 308 (C)?

A 308 (C), I had not quite gotten through with "B", had we.

Q Oh yes, we had finished "B" I think had we not?

THE CHAIRMAN: The second page.

MR. FRAWLEY: Yes, that is right, I am sorry.

A I believe about the last thing we were discussing was the 9.1 cents per gallon as the average return to the refinery for each gallon of gasoline regardless of grade, that was sold to the jobbing trade.

Q Yes?

A And I think I pointed out that if we did a break-down of this figure into the three different grades of gasoline and then figuring it back we would have the same composite average as we get this way, that for the purposes of determining the refinery spread there is no utility in analysing whether it is third grade, standard or premium grade gasoline, it all comes back to the same figure.

Q Yes, and I would like to and I would like, after you have said everything you want to say about this sheet, functioning as demonstrating the refinery spread, then I would like to go back to that again, to the discussion we had this morning?

A All right. Now the same method is applied to the refined oil, there is no necessity of going through it in detail but it shows for the jobbers that the price is 11.61 cents, in the aggregate for all of the refined oil sold from the Calgary refinery and for the tractor distillate it figures at 7.01 cents and for the light fuel oil you will notice

there is quite a difference, that is all of the sales of light fuel oil as sold to jobbers brought back a return averaging 15.10 cents per gallon but that a relatively large amount of that, by all odds the major part of it, was sales of outside purchases and if I understand the situation correctly, these outside purchasers were sold in territories where the price of the light fuel oil was relatively high and that there was very little sale relatively speaking of light fuel oil from the Calgary refinery and what was sold was sold at a much lower price than that 15 cents. It figures out that the average price of the light fuel oil as produced and sold from the Calgary refinery is 6.22 cents.

Q Yes.

MR. FRAWLEY: Now I think Mr. McGrath had better, for the record, he made this statement for us the other day and if you do not mind you might explain that further discrepancy, Mr. McGrath.

MR. McGRATH: The outside sales of $726,321---

Q MR. FRAWLEY: Gallons?

A Gallons, for which we received $117,709.65 was the sales of light fuel oil in the North West Territories produced and sold by the North West Company and as the accounting is done in the Calgary office or in the Edmonton office it has been, it was incorporated in the Edmonton sales and in this method we have eliminated the sale of that product; in other words the North West Company did not do any accounting, they had no money as a matter of fact, they sell the products and the accounting is done by the Edmonton office and that is how it happens to be in this figure, otherwise it would be stripped out and would not affect the figures one iota.

there is quite a difference [illegible] the [illegible]

light fuel oil as sold [illegible]

[illegible] 10 cents per [illegible] respectively

[illegible]

[illegible] of light [illegible]

[illegible] fuel oil as [illegible]

in [illegible].

[illegible]

letter, for the record, to make [illegible] statement [illegible]

[illegible] day and [illegible]

[illegible]

[illegible] which we [illegible] the [illegible]

[illegible]

sold [illegible]

[illegible] in the [illegible]

[illegible] the sale of that product [illegible]

[illegible] did not do [illegible]

[illegible] matter of fact, they [illegible]

[illegible] by the [illegible]

[illegible] this figure, otherwise [illegible]

[illegible] affect the [illegible]

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Q (MR. FRAWLEY TO DR. BROWN) That is the explanation you wanted?

A That was what I was trying to say. Now bunker fuel oil was not sold to jobbers and is shown as the price to the marketing department as 3 cents; the refinery consumption is the value of the refinery gas and fuel used in the refinery operations and because that gas is credited as one of the products of the refinery operation it is in here as 1.34 cents per gallon and similarly the asphalt and coke. Now the total gallons, we will find it is the last column, includes crude naphtha total sales, the last item of 2,609,416 gallons, which does not represent products made from the crude which is processed at the refinery and should not be included in getting the total gallons processed at the refinery; furthermore there is some coke which was sent to Regina to the extent of about, is it 70,000?

MR. McGRATH: 70,050.

WITNESS: It does not show on the sheet.

MR. McGRATH: That is right.

WITNESS: So that the total gallons shown on the last column will be the sum of all the items except the last one and the addition of 70,050 gallons, making a total of 68,568,351, which----

Q MR. FRAWLEY: Instead of 71?

A It will make the total of 68,568,351 instead of the 71,000,000.

Q THE CHAIRMAN: What are those figures again?

A 68,568,351, which is in check or in agreement with the total sales shown on Exhibit "308" A, the first column, the difference being the 70,000 different gallons of coke which was sent to Regina, it appears on "308" A, but it is not included

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on "308" B, which should be added in, and the 2,609,416 gallons of crude naphtha, which is on "308" B, but is not on the refinery production, Exhibit "308" A, because it is simply material brought in and sold without really being a refinery production, so that these figures are in agreement with those explanations.

Now the next page, "308" (C), shows how those returns were used in determining the refinery spread.

The last price given per gallon under each of the various items of "308" (B), is repeated in the third column of "308" (C). For example the product gallon was found to bring an average net return of 9.10 cents on Exhibit "308" (B) and 9.10 cents is listed under the 1938 realization in the third column, the second column of figures, on "308" (C).

Q Might I interrupt, you are now using the 9.1 cent which we find on "308" (B)?

A Yes.

Q To be the average realization on gasoline from jobbers?

A That is right.

Q But you are taking the figure of gallons which you are using of 42,745,113 as what?

A The total production from the refinery.

Q Both to the marketing department and to jobbers?

A Yes, in other words, we are pricing the entire production at the average price received from the jobbers.

Q That is it, this is where you are referring to Mr. Halverson as a jobber?

A Yes, at least he is not part of the refinery, put it that way.

Q That is right?

A The refined oil is 11.61; the tractor distillate 7.01; the light fuel is not given there. I have lost that.

MR. McGRATH: There was a reduction in price on light fuel oil this year, the early part of this year and we showed Mr. Cottle the figures on that and I think he was content with them, is that right.

WITNESS: Then the figure on the light fuel oil-----

MR. McGRATH: And the bunkers, the same way, there is a slight reduction on that.

WITNESS: Then the figures for the light fuel oil and the bunkers do not represent the price during 1938.

MR. McGRATH: That is right.

WITNESS: And therefore no price is listed in the 1938 realization.

MR. MCGRATH That is right.

Q (MR. FRAWLEY TO DR. BROWN): Can you get it by simply dividing the two?

A No, it is right there, Mr. Frawley, under the 1938 realization there is no figure given for light fuel oil and for bunkers.

Q In the "308" (C)?

A That is right but if you go over three more columns you will find under realization, including blending stocks per gallon, you will find 4.55 for the light fuel and 2.772, which I understand is the realization used for those two products, but that is not the 1938, that is the current realization for those.

MR. McGRATH: That is right.

Q MR. FRAWLEY: I do not see it at all, can you take---

A The figure on "308" (B)----

Q Can you take the 4.55 and move it over?

THE CHAIRMAN: Not without a different heading because it is in 1938.

A That is right.

Q MR. FRAWLEY: You could do this though , you could take under, across the line opposite light fuel oil, you could put 6.22?

A For 1938.

Q For the 1938 realization?

A That is right.

Q And then something in red showing the price adjustment in June, 1938?

A No, not in June 1938.

MR. McGRATH: In 1939.

Q MR. FRAWLEY: Well some price adjustment to be taken away at some date?

A It would be 1939, would it not?

MR. McGRATH: That is right.

Q MR. FRAWLEY: And then something for selling expense and then come to 4.55?

A That is right.

Q All right?

A And the same statement would apply exactly to the bunker fuel, that is the price used is not the 3 cents or any other figure shown on "308" (B) but is a price representing that currently received for the bunker fuel.

C2
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Refinery consumption is carried through at a constant value of 1.3400 cents; the asphalt is in at the 8.61, which represents the price received from their own marketing organization as no asphalt was sold to the jobbers and coke the same way, 2.5900, and then the loss of 4,158,593 gallons is also added in and we have as a total gallons produced, 68,491,811, including losses; to that is added the unfinished stock and we get a figure of 70,407,571, which is the same figure as appears in the last column of "308" (A) which is the production, including blending stocks and loss.

Q In the year 1938?

A In the year 1938, which again ties the various Exhibits together.

Now the 1938 realization on gasoline is shown as 9.1 cent. That is the actual average realization received during the year 1938. In June 1938 the price was decreased so that there is a correction applied to this figure of 9.1 cents to bring it down to what the average realization would have been in 1938 if the price structure as existed from June to the present date was in effect.

Q Why do you do that or why did they do that?

A That was done to bring all of these realizations up to the present current conditions as of June, 1939.

Q The last half of 1938 being the same as the year 1939?

A The same as the present.

Q It was to give the Commission the present day picture that that adjustment was made and you shought to find out, and

this whole Exhibit "308" (C), does seek to demonstrate what would have been the realization if that reduction made in June 1938 had been made on the 1st of January, 1938?

A That is right. In other words it represents actual present conditions on the assumption that the same throughput is going through the refinery now as went through in 1938, or to put it the other way, what would have happened in 1938 if the prices during the entire year 1938 were as they now are.

(Go to number 9060)

Q In other words, you would have only for the Commission a picture with a refinery spread and a refinery profit, as of 1938 which could not have well been taken as today's experience, but this exhibit here has been an attempt to permit the Commission to quite safely take the statement as representing today's operations?

A That is right, and this figure in red under the Column Less Price Adjustment June 1938, which is 42/100ths of a cent for the gasoline, is that correction or adjustment made in the average price actually received through 1938 to make it equal to the price that would have been received under these conditions we have just discussed. Similarly the 2/100ths for the refined oil, and for the tractor distillate, for the light fuel oil and bunkers, the current price is given in the next column under realizations, and no adjustment is made in those. Refinery fuel is evaluated the same price. The column of red figures with small numbers varying from about 1/100th of a cent for the tractor distillate up to 18/100ths for asphalt, represents loading which was included in the 9.1 cents, for the staff required to keep records and look after the sales to the jobbers. It is properly a Sales Expense and the accounting practice of the Imperial has been to take all of these Sales Expense items out of the refinery operations. I believe you may recall I mentioned the other day that the common practice in the States is usually to include certain Sales Expense and this is consistent with the statement I made the other day that there is no Sales Expense included in these refinery

spreads and in these refinery figures as given. So that the net realization under these current conditions for 1938 production would be as listed in the next column under head "Realization, Including Blending Stocks per Gallon," which is 8.66 for the gasoline and 11.29 for the refined oil, and so on.

Q You say that there is no inconsistency between our finding the .02 cents called Selling Expense for Gasoline at this refinery and your statement yesterday that you found nothing charged to the refinery for Selling Expense, and for that reason you felt that some of that Head office Expense was properly charged against the refinery. But I see it is called Selling Expense. That should be clear. That is perhaps not just what it means.

MR. McGRATH: That is correct. That is not Selling Expense. It is Accounting Expense you might term it. I headed this Selling Expense, but it is an Accounting Expense.

MR. FRAWLEY: Then it is charged for loading, as we now understand?

A As I understand, it is an expense incurred due to keeping records of these jobbers' sales.

Q However much of it is kept at this refinery?

A Yes. It is not included in the refinery cost of operation nor in the refinery returns in this analysis.

Q THE CHAIRMAN: And does not purport to cover sales, the cost of selling?

A No.

Q Although the word "selling" does appear in "308-C", that is a misnomer as I understand?

[illegible]

[illegible] that [illegible]

[illegible]

MR. McGRATH: That is correct.

THE CHAIRMAN: And the word "selling" should be changed to "accounting"?

MR. McGRATH: Accounting.

A Accounting for Sales, that is really what it is.

MR. McGRATH: Yes, that is what it really is.

MR. FRAWLEY: And loading?

MR. McGRATH: No. That is in the Refinery Expense.

MR. FRAWLEY: All right.

A So that the realization, including blending stocks per gallon, given in the next column, gasoline 8.66 and refined oil 11.29 and so on. Now then, to find the realization that would have been actually realized in 1938 on the basis of current prices, we then multiply the gallons of gasoline produced in the second column, 42,745,113 by this realization of 8.66 cents, and that is carried over into the figure $3,701,726.79.

THE CHAIRMAN: Where is that? Oh, the first figure. This one?

A. Yes, multiply this quantity by that and it gives this.

Q Yes?

A And that gives us the realization on this basis of 1938 production to current prices. Now in that gasoline you will note that all of these realizations bear, there is included blending stocks, and in that gasoline that was sold there was included Ioca naphtha and Lead Tetra-Ethyl and some.....

Q Solvent oil?

A Solvent or lubricating oil. These materials were not

produced by the refinery, but are simply purchased and are brought in and blended with the gasoline and sold as part of the gasoline. Therefore, they should not be included in the refinery production.

Q Why?

A Because they were not produced from the crude oils nor the naphtha nor the casing head which was processed in the refinery, but are outside purchases brought in and items not processed in the refinery but simply blended with the gasoline in order to make it marketable.

Q THE CHAIRMAN: Why not a blending cost?

A Well, the cost of blending is assumed as part of the operation of the refinery. But ther is no processing done of these materials. It is just as though they bought some dye to colour the material green or red.

Q MR. FRAWLEY: Well, that is perhaps in there because they do buy dye, lead and dye goes together?

A Lead, dye and Ioca naphtha and this lubricant oil.

Q I know what you are doing, but just why are you doing it?

A I am doing it so I can find out how much money was received at the refinery gate for that material which was produced from the crude oil and crude naphtha which were processed in the refinery and I do not want to include in that item the money which was received for dyes, lead, Ioca naphtha and things of that kind.

Q In other words, you might just as well say "We are selling you some gasoline without blending stocks or dye or lead, and we are selling you that along with it.

In the price that we charge you there are these two things," but at the moment we are only interested here, at least we are not interested here in the transaction which essentially was the sale of blending stocks and the dye and lead?

A That is right.

Q Why are we not?

THE CHAIRMAN: I can quite follow that you take the crude and you follow it through the refinery until it comes to the refinery exit door, and you put your figure on that, what has happened in between?

A That is right.

Q I also follow Mr.Frawley's suggestion that when you take this lead and other products of which you speak and put in that gasoline you sell, that you are selling that of which you have spoken and you are selling these other things as well.

A Yes.

Q I follow that too. But I do not yet see, since it must cost money to properly intermix this foreign product after it comes into the refinery door, and which went out of the other door, why the refinery should not properly make a charge for that operation of mixing?

A That is done. That is still in there. That has not been taken out. It is simply the cost of the dye and the lead itself which has been subtracted along with the quantity of the lead and the dye. Whatever cost is incurred in handling the lead and the dye in the refinery is still charged against refinery

operations.

Q Yes, I see. So that it is there although it is not there as a separate item.

Q MR. FRALEY: It is in the refinery costs that we already discussed?

A The cost.....

Q Of doing these things, mixing these up?

A The cost of blending is in there. The only thing that is taken out is the cost of the material which is blended and the quantity of the material which is blended.

Q Suppose that a refinery customer said "Well, give me the blending naphtha, the Ioco and the lead and the dye and the solvent oil, but give these to me separately. Put these in a separate barrel for me, and sell me a barrel of gasoline and then sell me some of these other things and I will blend them myself, after I get them out of the refinery door." How would that be reflected?

A The refinery does that very thing, but it says "No, we will blend them for you, it is easier." That is exactly what they do?

Q Yes? You feel that the refinery is selling them a lot of things. Selling them gasoline made of the crude and selling them some blending materials?

A Yes.

Q You take that away, the cost only of the blending materials in order to arrive at a true refinery realization for the gasoline that they made from the crude?

A That is right.

Dr. G. G. Brown.

Q MR. COMMISSIONER LIPSETT: This Ioco, Dr. Brown, that is another Imperial product made by one of their own companies?

A Yes. It is not produced at the Calgary Refinery. I am not sure whether it is produced bby one of their companies.

MR. McGRATH: Yes, it is produced by our own refinery at Ioco, British Columbia.

A It is not produced in the Alberta Refinery, nor is it produced from Turner Valley crude. It is an entirely separate material. Insofar as Calgary refining operations and Turner Valley crude goes it should be handled the same as any other outside purchase.

Q MR. COMMISSIONER LIPSETT: Have you considered whether the charge of $512,000.00 for that Ioco and the Tetra-Ethyl, whether that is correct?

A That is an actual expenditure. That is put in here as an actual expenditure. I am not going back again to audit their books or anything of that kind. But that is a perfectly proper figure because Tetra-Ethyl lead costs something like $8.00 a gallon.

MR. McGRATH: Yes.

A Or $8.50 a gallon. Lead Ethyl is very expensive. So that the cost of $512,000.00 might look large because it includes the cost of the Ethyl fluid which is very expensive and also the Ioco naphtha costs more than gasoline produced from Turner Valley. That is in Exhibit "280", Schedule 4.

Q THE CHAIRMAN: What is concerning me some, is the approach to the problem that you

are making at the moment, making use of these figures. You say in effect this, as I understand you, Dr. Brown, that having regard to all of the operations which are undertaken in a refinery to convert the crude product into the refined products which emerge after the refining process, you ascertain the cost of operating. You get the operating expenditure upon which you pass. You take into account the capital expenditure?

A As determinigg depreciation.

Q As determining the depreciation which will find its way into operating again?

A Yes.

Q For amortization purposes. And you say having verified these various items, if we can, we then find what the net profit in the operation is?

A Well I have not gone quite that far yet.

Q That is our approach is it not?

A It is on this page but we have not got down to it.

Q Quite so. You find that net profit and then that leads to the conclusion one way or the other that the price charged is not unreasonable in the sense that any less price would provide an improper return on the capital investment?

A That is right.

Q Or vice versa that the profit is so great that the other aspect must obtain?

A Yes.

Q That is your present approach?

A Yes. With this one further explanation that it is based not on the actual conditions as they were in

Dr. G. G. Brown

1938, but upon the actual price structure as it now exists put back on the throughput and production of 1938.

Q Quite so?

A We are trying to bring it up to date so that it is of immediate practical value.

Q Quite so. Is not that a pure accountancy approach?

A Yes.

Q From the historical standpoint?

A Yes. This is factual. There is no estimate in here at all.

Q Quite. But having regard to your wide experience and assuming again that you are concerned with the interests of a plant, would you think that approach would best give the picture of realities?

A Yes, that is the best approach I think towards getting realities as they now exist.

Q You think that a better approach than saying "I know that in an efficient plant, economically conducted, gasoline and the other products enumerated should be turned out for so much money and anything procured over and above that is unreasonable if one is concerned with the interests of the consumers as well as the refinery." Is that a sensible approach?

A Yes. But in order though to reach that conclusion I must start either with some assumed conditions or some conditions as they do exist, and these are the conditions as they do exist. Now, I am taking the conditions as they do exist and figuring out what the fair operating conditions would be at the present time with conditions as they actually do exist. In other

Dr. G. G. Brown.

words, my client, coming in here, has to actually receive gasoline, not hypothetical gasoline that might be produced if there were some other plant here, but he must get the gasoline from the plant that is now in existence. This is the plant which is now in existence in supplying most of the gasoline used here. Therefore it is a condition as it exists. Now the other question might be whether or not my client might be advised to put in his own refinery and make his own gasoline because he might have got it cheaper. That is another question but that is not the one you put to me yesterday.

Q Now, supposing your client was charged with the responsibility of deciding what was a fair price and he came to you for advice. He is not a refiner. He has no interest. The fact is that the jobber must pay so much. That is a present fact. But he says "There may be a situation here of economic domination."

A That is right.

Q "Everybody in this territory may say that is what the jobber is going to have to pay if he gets anything from a refinery in this territory", but your client may say "Well, is that right. I find that in other territories people are getting their products for much less money, and I do not care at all about the fact that the jobber here has got to pay. Should he have to pay, that is what I want to know?"

A That is right.

Q How would you approach that?

A We can approach it in any one of a number of different

[illegible]

ways,

Q I am wondering what is the best approach?

A We can only approach it one way at one time.

Q As you are doing?

A Let us take one way first, and the way we have now started to approach that is that here are the facilities available in Calgary for producing gasoline, and this is the cost of crude and this is the cost of crude naphtha, and this is the cost of absorption naphtha, and this is the cost of Ioco naphtha and this is the cost of lead Tetra-Ethyl and this is the cost of other blending products. This is the operating cost of that refinery. We take all these things into consideration and we find that the refinery selling gasoline at the present price is making so much money. Then he can say "That is too much money for them to make," or "Well, I would not operate unless I could make more money than that." I do not know what attitude he is going to take. That is up to him. He makes up his mind that is only a fair return for that particular operation, and then I say that is the return this refinery has to get. If you think that is a fair return under these conditions, then the present prices are fair prices under the conditions as they exist. That is one approach and one answer. Then you opened the door to another approach and you said "But somebody out here in Saskatchewan is getting gasoline at a lower price." I say "Ah, but that is not in Calgary. Why do I have to tolerate conditions as they now exist in Calgary. What other conditions might exist in Calgary which would give me gasoline

at a lower price?" Then he says, as you did this morning "Would you lay out a plant on paper and estimate its cost, its operating cost to produce so much gasoline and see if I can make this gasoline cheaper myself." That is another approach.

Q And you say, having done that, and bearing in mind our supposititious client, having done that you say "I do not run the same chance of being lost in a maze of figures. I test them by....."

A By experience.

Q By this additional method. But there is yet another approach, is there?

A Yes, there is another one which you might wish to consider. And that is this client of mine is coming in and he is going to use more gasoline than has been used in the past. He is an additional market. He is going to say "Well, if I go into that market and take more gasoline than has been processed and produced in the past, the cost of producing that additional gasoline may be less than it was for producing the smaller amount and I may be able to go to the present refiner and say 'Now I want so many million gallons next year, and if I take that right at your gate and no guarantees of quality except your regular grade and so on, what can I get it for?'" He might get it for a lower price because the cost of the production of that extra amount of gasoline will be less than the cost of the production of the gasoline that would be produced otherwise, and the very fact they are processing more crude will doubtless decrease their cost per barrel

of crude and, therefore, it will decrease the cost of all of their production. So that man coming into this territory says " I am improving the efficiency of the present refining operation because I am taking more gasoline. Therefore I should not pay the present price. I should pay a lower price." As a result of his coming in and taking more gasoline the whole territory may get a lower price. I believe that is really what happened in June 1938. There was a good year here, a large throughput through the refinery and they were processing crude for the British American as well as their own and they found their costs were lower than they had ever been before, and down came the price to everybody.

Q So that a recommendation having to do with the present price must not lose sight of the possibility of an increase or decrease in throughput?

A Right. Now these three approaches and these three answers must all be weighed by this client. I will (1) go in and buy on the market as is. That gives a fair return, apparently, on the structure as it now exists. (2) Or, I will go and build my own plant and process a small amount of crude. It will cost me as much or maybe a little bit more than I can buy for now on the market. Or, if I go in and give my business to (3) the present company so that they can operate more efficiently, they ought to perhaps cut the price a little bit to me.

Q And it is a matter then, having given thought to all of these methods of approach, he makes up his mind what to do?

Dr. G. G. Brown.

A He weighs and balances all these factors that must be weighed to come to a conclusion.

Q And if the approach by way of figures only stands the test, when weighed with other methods of approach, you may feel sure that the conclusion predicated upon the historical accounting method is the sound one?

A You would, I think, perhaps want to explore all three of these.

Q I am sorry to interrupt you, but I just want to be clear in my own mind.

MR. FRAWLEY: It is very useful.

(Go to Page 9074).

THE CHAIRMAN: I am sorry to interrupt you but I just wanted to be clear in my own mind.

MR. FRAWLEY: It is very useful.

Q MAJOR LIPSETT: Why do you, Dr. Brown, have to go to, if you found that there was to all intents and purposes a virtual monopoly of the crude supply and also of the refining in one or two or three strong hands, might you then not have to approach it from a point of view of what the fair price for the refining and all this, and then form your own estimate, apart altogether from this client who here hypothetically would seem to have some independent market?

A Well these three methods that I have outlined are really independent of whether there is an independent market. Really I think you have outlined rather a modification of this first principle that we just discussed, that is supposing all the crude is owned by one company.

Q Yes?

A And supposing that some company operates the only refinery which is there.

Q Yes?

A Well this client who is coming in would then have to see if he could make a contract with that refiner which will give him what he considers a fair return and if they are not reasonable he then has to find out whether he can get the gasoline somewhere else, whether he can get some crude and process it himself or whether he is going to keep out of Calgary altogether; in other words if he cannot buy crude then of course he cannot put in his own refinery and if he feels, after studying it, that the price asked by this monopoly is too high, he either will refuse to pay it and

not come in with his business or else see if he cannot get a special contract. It seems to me that that proposition of monopoly does not enter into the study as we are now approaching it regarding the refinery cost and what is the fair price. The monopoly or competitive conditions are primarly factors which might control marketing, that is the marketing through the various distributors and the people who buy gasoline; in other words whether you have a monopoly or not, the cost of producing the gasoline from crude is going to be the same in the same plant operated in the same manner; that the considerations of monopoly and competitive conditions are truly applicable only when you begin to consider the marketing and what is actually obtained through the marketing processes for the products; that the costs of production of gasoline is not controlled by whether the refinery has a monopoly or not.

Q THE CHAIRMAN: Because it is not affected by what you pay for your crude?

A That is right.

Q But ultimately the customer or the consumer is very much affected?

Q Yes.

Q But for the immediate problem of the refining, it does not matter?

A No, in other words we have not divorced the marketing problem entirely from the refining problem and the price that the refiner might receive for his gasoline is in turn dependent upon the marketing situation and that is where the monopoly factor comes in, is when he begins to sell his gasoline. It does not come in as an important factor at all in the production

of his gasoline from crude at a certain price. In other words the Imperial refinery, if that were the only refinery in this territory, and had a complete monopoly, its cost of production would be the same as long as it was operated in the same manner, whether it was owned by a company that had a monopoly or whether there were other refineries in the same territory. The controlling factor of the cost of refining is not the organization which owns the refinery but the equipment and the efficiency with which the equipment is operated and the quality of crude which is processed.

Q MAJOR LIPSETT: I suppose you could really put it, a little further in this way, that if there was only one refinery that had a very large volume, its costs might be a little less than if there were two or three refineries turning out that volume?

A Yes, very much so. I think I can give you an estimate that is founded upon the same figures, that the refining costs of the Imperial Refinery would have been increased about 14 cents a barrel if in their operation they had not had the benefit of processing the British American's crude during the year 1938; now that is due simply to the fact that they were enabled to operate their plant at its maximum capacity throughout the entire year and if they had not enough crude they would still have to keep their plant in working order, they still have to keep their forces on the job but they do not have as much crude going through the refinery and the overhead has to be borne by the smaller quantity of material being processed. Now that is a factor which determines the cost of producing the gasoline and as I see it the consideration of monopoly and competitive conditions are of prime

consideration only in the marketing problem.

Q THE CHAIRMAN: Well would you say "only in the marketing problem", would it not be more proper to say that it does not affect refining costs because something more than marketing may affect the consumer price, namely the cost of the crude products that you take in at the refinery door, supposing they are entirely separate people?

A The refiner and the crude producer.

Q Yes?

A Quite.

Q It would make a big difference to the ultimate consumer what the cost of the crude product was?

A That is right.

Q And the cost the refiner had to pay?

A Yes, well I was looking upon that----

Q Without touching the question of the operation of refining at all?

A I think it would be better, in other word the question of monopoly or competitive conditions has practically no effect on the actual refining costs.

Q Yes?

A And that is what we are really considering now.

MR.FRAWLEY: Yes.

Q MAJOR LIPSETT: That would leave open this question of whether there was a monopoly of crude production or what was the fair cost of the crude, or all the material, any other raw material, you first approach the actual refining costs as a matter which would not be affected, monopoly or no monopoly?

A That is right. In other words the refining costs may be, of

1938, or present prices, say 45 cents a barrel. Now if the crude costs a dollar a barrel it would then mean that the refiner would be able to produce his finished product with an average price of $1.45 per barrel, while if the crude cost him $2.00 per barrel, the refining would be the same, 45 cents a barrel, and he must get a return of $2.45 per barrel of crude in order to meet his operating expenses and any excess profit and anything of that kind to the refiner would depend upon what he was able to market his products for and that again is a marketing problem.

MAJOR LIPSETT: Thank you.

Q MR. FRAWLEY: In other words, we have heard a lot about the advantages of the intregated company; I take it from what you say that, rather as to the refining operation alone, there is no particular advantage in being intregated, now is that sound or what are your comments on that?

A If I understand your question correctly, the answer is "Yes", but the advantages in being intregated are primarily that under certain conditions there may be no profit in marketing retail materials; in other words there may be conditions such that the refiner ..as to sell his production at a very low price, during that same period there may be a profit in producing crude oil.

Q In other words the intregated man has three places to go to find his profits?

A Yes, and if two of them fail him, he may be able to keep his head a: ove water with the third one.

Q There is another one I want to put to you, I take it from what you have said that you do not find the Imperial Plant

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

in Calgary to be a particularly inefficient one,-rather the contrary from your observations this morning,-and I am summing up your evidence correctly when I say that, from your evidence that you find the Imperial's plant certainly on its 1938 operation, efficient?

A I think so.

Q Now take the contrary, if we find to be a fact, if you came in here and found that this Imperial operation, sitting as it does in the picture with no other large refinery in operation, and you find it to be completely antiquated and obsolete, what would be your views in the light of what you have been discussing with the Chairman a moment ago and what would be the problem then facing the Commission, if we had the actual situation and the facts were that there was a very antiquated and expensive operation here of refining crude, nevertheless it would be the fact and the only fact, putting it to you as you put it to yourself some moments ago, what would be the problem then?

A Then we would take the second basis or the second step, that is we find my client coming into this territory and constructing his own refinery because he can operate his own efficient plant at a lower cost than the cost of this inefficient plant upon which he might otherwise have to depend for his supply.

Q Yes. Now getting away a little bit from the parallel----

Q THE CHAIRMAN: That brings in the element, if I may interrupt, Mr. Frawley?

MR. FRAWLEY. Yes.

Q THE CHAIRMAN: That brings in the element of reducing the throughput by means of competition, does it not, Doctor?

A Yes.

Q Is there not another picture still than those which we have been considering, namely, or another method of approach rather, namely, what an efficient substitute plant would do, not a competitive plant, a substitute plant?

A A single plant.

Q Yes?

A Supplying the whole territory.

Q Having regard to particular plants you are considering, there may be competitors here already now, but you are considering a particular throughput, a particular situation and you are examining it at the moment for a particular company?

A Yes.

Q Now then this suppositious client, if he came in himself and got some of the business, he would reduce the throughput and would not hope to get all of the business, and so there would be a different situation, having regard to the considerations of volume to which you have alluded?

A Yes. Well now that would----

Q What about the efficient, your suppositious case is, this refiner's capital expenditure, it cost so much, all right, if it were an efficient, up-to-date plant, what would be the capital expenditure and what would the operating costs be?

A Well that puts us into this third study or the third approach.

Q That is covered by the third is it?

A Yes, and if I may elaborate on that a bit perhaps I can make it clear. My client coming into the territory sees an inefficient plant, he thinks the costs are too high, the price is too high. He first gets a report on whether or not he should build his own plant to supply his needs. That does not look too good to him. He says "Let us go over to this

[illegible] another who are still [illegible]

[illegible]

[illegible] plant, [illegible]

[illegible]

[illegible] whole territory.

[illegible]

[illegible] be competitors [illegible]

[illegible] particular throughout, [illegible]

[illegible] it at [illegible]

[illegible] supported [illegible]

[illegible] would [illegible] get [illegible]

[illegible] different [illegible]

[illegible]

[illegible] efficient, [illegible]

[illegible]

company who has this inefficient plant and see if we cannot make a contract with them. We will take so much and will give them such a contract", and they go and talk to the head of the company and the head of the company says "We cannot do that right now. Our plant is not equipped for that", and they say "don't you want the business , and if so why don't you make your plant capable of handling this extra business", and the answer is "Yes, if we had the capital to do it." "Well here is a contract, cannot you take this contract now and go to your banker and raise the money and put in a modern plant" and that is what they do, because he has come into the territory and has supplied a constant market which will enable them to put more crude through their plant. Then they decide to rebuild their plant on an efficient basis and give him his gasoline for what he would regard as an equitably low price and by so doing the whole territory is benefited. It is a modification of what I outlined a few moments ago. I really believe that so long as we consider private enterprise or refineries operated on a more or less competitive basis, that these three methods of approach will cover the situation.

There is of course one other possibility which I thought might have been in your mind but which opens up a question again as to whether or not this should be made a public utility and that would be to take all the refineries which we have and scrap all of them and build one large plant which would operate as a common refinery for all of the market. Now that is really a question which I think is a little separate and distinct from what we have been discussing because it means a complete change in the economic society insofar as the refineries go.

Q Yes?

A But perhaps you might want to consider it.

Q Well we are rather hoping to benefit from your advice as to how to answer concrete questions. We do not sit as a Board to determine as to whether or not there should be Government intervention or not but to make recommendations as to "is this price fair", "is that price fair", "is this just", "is this equitable", hence my anxiety about examining into the methods of approach because we must give answers?

A Yes.

Q We are not in the very least concerned with such questions as Government ownership, that is for an entirely different body elsewhere sitting, but we are concerned with making appropriate answers to the questions submittted and they involve "is the price fair", well as you approach it, you may think something is fair from the standpoint, for example, what is fair to the producer of crude oil in Turner Valley, that is one thing?

A Yes.

Q But what is fair to the consumer when that product is converted into gasoline may be a wholly different thing and we may be troubled with the very troublesome question of who are we being fair to and it is in like considerations to that as to which we are seeking help from such men as yourself rather than saying "What do we want to know"?

A Well take this question of whether the price is fair or not, there must be some basis upon which we are to pass judgment.

perhaps you might want to [illegible]

[illegible] rather [illegible]

[illegible] with such questions as

Government, wherein, [illegible] of France [illegible]

knowledge fitting, [illegible]

plain answers to the [illegible]

"this right", [illegible]

But what is fair to [illegible]

[illegible] scientifically be wholly [illegible]

[illegible] with the very [illegible]

[illegible] it is in like [illegible] that [illegible]

[illegible] this question [illegible]

there must be [illegible]

Q Yes?

A And once that basis is set up then we can arrive at the answer, but until that basis is set up then we cannot arrive at an answer.

Q But an expert comes in and says, in this case, as I am understanding you,"For the moment I am taking the historical accounting method of approach, which I shall test by all these other means and then I hope that I can give my client an intelligent answer and my basis of approach is not any one in particular but each one tested by the other"?

A But each one examined independently on its own basis and then the comparison made.

Q Yes?

A In other words I believe that it would be impractical, if not impossible, to just put the crude oil and the refinery and the marketing and the consumer all in one pot and stir them up and look at the whole picture and say "Now we are fair to everybody". I do not think we should get very far that way.

Q Quite so?

A But we can do it this way, we can say "Now under the conditions as they now exist in Alberta, with crude to the South of us and crude to the North of us, and around us, what is the fair price for the crude oil on the basis that the Turner Valley crude oil will supply the needs, almost en toto, of Alberta and be used at the refinery at Regina," that will enable us on that basis to arrive at a fair price. If however you want to take a different basis and say "now what would be a fair price for Turner Valley crude on the basis that that crude is to be used down at Sarnia in competition with Illinois crude", you have an entirely different figure.

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G. G. Brown

Q Yes?

A Now, there is another basis which a good many people think about, which is an extremely difficult one to use, and that is on the basis of getting the crude out of the ground. You may find that the cost of getting the crude out of the ground varies tremendously for the different producers and from year to year.

Q Yes?

A And the same thing is true to the refiner except that in a refinery we have an operation where we can arrive at the cost of processing, and again that cost of processing will depend upon the amount of crude put through the refinery, and the question is now "What is the fair price for gasoline, kerosene, tractor fuel", and so on, on the basis of the Imperial refinery as it now exists, operating at the rate as existed in 1938 but at present prices. We can get the answer.

Then there is another problem, what is the probable fair price for the gasoline and other products produced at the Imperial refinery at the present price but operating it at one-half the rate of 1938, and we can get the answer. But to just take the thing in its entirity and get an over-all answer will lead to confusion. Now, I think if we can take this problem and break it down into its parts, analyse it from one stand-point and another stand-point, if we agree to set up some hypothetical condition, then you will be in shape to answer the questions which you may have to answer, because we will set up the conditions which are likely to be encountered.

Q I understand then, Doctor, you say at the moment, "I am engaged in the question of refining costs" ?

G. G. Brown

A Yes, on a certain basis.

Q On a certain basis, and I am arriving at my conclusion after having approached the problem presented by different methods?

A But now I am doing only one method right now.

Q Right now?

A Yes.

Q And we are interrupting it, I know?

A No.

Q But I am trying to get this clearly?

A I am very glad to have the opportunity to get my ideas in your mind, because I feel you will not understand what I am talking about unless you do have them, and what I am trying to do here is to analyse the present Imperial refinery as it is now constituted, operating under the present price structure as it now exists.

Q Yes?

A But at the rate that it did operate in 1938.

Q Yes?

A Now that answer will be applicable to those conditions only.

Q Now I am stepping aside for the moment from your immediate problem, to our larger one, to get the benefit of your very wide experience in connection with it, as I understand you, supposing you had to come to a conclusion today, after approaching the problem by the methods which you have mentioned, that particular problem, you would come to an opinion, but you would want to know before, before it went into the jobbers' hands, at what price

G. G. Brown

the refiner has bought his crude, of course, because that would have to be added?

A Yes.

Q To the refinery cost in determining what the jobber should pay, at least the refiner would certainly add to his cost what he paid for his crude material?

A Yes, that is one of the factors which would determine the price at which the products must be sold.

Q Yes, I am trying to get the picture of the broad approach to the whole thing now, if I may, interjecting it, mind you, into what you are doing, I know?

A Yes.

Q So it would be important to anyone concerned with what the jobber should pay, to know if the price of crude asked for and obtained from the refiner, was a proper one?

A That is right.

Q And having gotten it into the jobbers, and that is something which we might have to struggle with, with someone else, you are not concerning yourself with that, as I understand you?

A No, I am concerned here with the operations solely at the present time.

Q And when you finish with the refinery, when the refinery is done with, then, assuming we knew about the proper price of crude.........

MR. FRAWLEY: May I interrupt, Mr. Chairman, Dr. Brown is going to discuss separately the value of crude.

THE CHAIRMAN: Oh, I see.

MR. FRAWLEY: The value of crude separately.

THE CHAIRMAN: I see. We come to that, then,

but I want to know where we are at, to try and see if I can sort out this whole question merely as to the approach, not in detail, you get then the price of crude, you get the price of refining, the proper one, and then you should have the proper price to the jobbers?

A That is right.

Q Then you have the proper price of marketing?

A That is right.

Q And you are into the consumer's hands?

A That is right.

THE CHAIRMAN: And you say, that Dr. Brown is going to discuss the proper field price of crude oil in this territory at this time?

MR. FRAWLEY: Is going to discuss certain aspects of it. He is going to discuss the value of that crude to the company at the Regina refinery.

THE CHAIRMAN: I see.

MR. FRAWLEY: In other words, he is going to discuss and analyse Mr. McGrath's Exhibit "283", I think it is , the Exhibit I gave you, no, Exhibit "268" the build-up of the price of crude starting with a dollar at Montana.

MR. MCGRATH: And $1.10.

MR. FRAWLEY: And $1.10, there are two of them.

THE CHAIRMAN: My interjections have unduly taken up your time, but I am trying to get it clear in my own mind, what the broad and general approach is.

MR. FRAWLEY: Yes.

G. G. Brown

Q MR. FRAWLEY: Dr. Brown, if you would leave for the moment this character which you have assumed at the Chairman's request, of advising a commercial client, and put yourself a little more in the position of perhaps what you actually are, someone called upon to submit an opinion to this Commission, just change it a little bit, suppose the Commission, charged as it is by the terms of this Commission, rather the Commissioners charged by the terms of this Commission, had called you in to advise as to how best to answer these questions, one of them being the proper refinery price, the fair and equitable refinery cost, and linked up with that, the fair and equitable refinery price, in other words what the tank-car price in Alberta should be, and you said "First I have to take the particular problem and I go to the particular company supplying the most of the market"..........

A Well, I would take conditions as they exist.

Q Yes, and that is why you have concerned yourself with this historical analysis of what the Imperial's costs are, costs and profits are, as refiners only?

A Because it tells me what the conditions are right now,

Q Yes, and there is a complete cut-off in your work at the refinery door?

A That is right.

Q Now you realize of course that the Commissioners are not bound to accept what may be a fact........

A That is rightt

Q Let us assume that you in pursuing those facts, found that on that Imperial operation, that refinery operation only, I am speaking of?

A Yes.

Q The profit that they made as refiners per barrel was not an unfair one, assuming that is so?

A Yes.

Q You appreciate of course that that does not end the Commissioners' problem, does it, you realize that?

A That is really the beginning.

Q That is just the beginning?

That is just the beginning. In other words, if the Commissioners, to goback to what I put to you a moment ago, if the Commissioners, while finding that that particular operation only showed a fair profit, they might very well say "Well, that particular operation is a too expensive one", that is so, is it not?

A That is possible.

Q So that is why, then, we are going behind what the Imperial has submitted here actually and historically with respect to their 1938 operation, and you intend to add to that, estimates in connection with the British American operation, the Mayland operation, the Lion operation, and a new one altogether probably, in other words, what I suggest you should do, if that is not one of the things which has already been suggested to you, that you should substitute for the actual Imperial plant, a better Imperial plant, if that to you as an engineer is possible, and show what that refining expense would be if there was in that Imperial, in that plant, a more modern and more efficient and more up-to-date plant?

A All right.

Q That is understood, is it not?

[illegible]

G. G. Brown

A All right.

Q Thank you very much. Now, would you mind just running through the balance of Exhibit "308" (C)?

A Well, I think we were discussing the deduction of the 1,375,174 gallons of blending stocks and their cost of $512,316.99, which had been deducted, both the amount of gallons and the amount in dollars, for the reason that those gallons represent materials purchased outside the refinery, not produced from Turner Valley crude, and are simply blending materials, such as dyes added to the gasoline, and after those subtractions have been made, we then find in the last two columns the net realization from crude and absorption naphtha to be 41,369,939 gallons ofgasoline because the additional amount of 1,375,174 gallons did not come from the crude and the absorption naphtha but from the blending stocks, and the amount received is $3,189,409.80, instead of $3,701,726,79, because the difference of $512,000.00 was received not for gasoline produced from crude and absorption naphtha but for the blending stocks such as the Ioco naphtha, leaded tetra Ethyl, lubricants and dyes, with the net result that the total of 67,116,637 gallons, including gasoline, refined oil and alloother products produced from the crude and the absorption naphtha, the coke and the loss, realized $4,299,229.30.

A and that is the realization that would have been obtained in 1938 from this quantity of crude run if the prices existing at the present time were in effect through the year 1938. Now the balance of this sheet is perhaps the part in which we have the most interest, because it leads us to the conclusion as to how much profit was made and also what the spread was per barrel on crude. This $4,299,229.30 representing the realizations has to be reduced by the cost of the crude processed, the absorption naphtha and the crude naphtha. It should also be reduced by the value of the inventory in January 1938 and it should be increased by the inventory of January 1, 1939, because if the refiner had been making gasoline during the year and putting it into storage and had not sold it the refinery returns should be increased by that amount. And that is done in the lower part of the page. The first items are the cost of crude and absorption naphtha consumed, at purchase price laid down at the refinery. There are Turner Valley crude consumed 58,000,000 gallons at $1.3770 per barrel. There is Turner Valley absorption naphtha of over 8,000,000 gallons at $2.1449 per barrel and there is Turner Valley crude naphtha, some 422,000 gallons at its price and some Pondera crude of over 1,000,000 gallons at its price laid down of $1.6135, making a total there of 69,032,397 gallons or 1,972,354 barrels. That figure is not on this sheet.

MR. COMMISSIONER LIPSETT: Give me the barrels?

A 1,972,354 barrels, which represents the quantity of material processed at the refinery and for which a total

[illegible] obtain

[illegible] quantity [illegible] times

[illegible] the average [illegible]

[illegible] before [illegible]

[illegible] move [illegible]

[illegible] calculated [illegible]

[illegible]

[illegible] requir[illegible] has

[illegible] the

[illegible]

[illegible] many

[illegible]

[illegible] more [illegible]

[illegible]

of $8,925,423.43 was paid for that material laid down at the refinery. Now in addition to what was processed during the year there was on hand at the beginning of the year, January 1938, the next item, which says "add opening inventory unfinished stocksless depreciation in inventory," of 6,059,445 gallons, which has been appraised in their semi-finished condition at a total value of $358,117.83. Then we should subtract from that the inventory on January 1, 1939, and its appraised value, which figures are shown in red as totalling 7,975,205 gallons and the appraised value $342,536.24. After making those adjustments we have as the total quantity of raw material used to produce the quantity of finished products sold of 67,115,637. I think that is the right figure or is it 15. I think it should be sixteen.

MR. MCGRATH: It should be 16.

A 67,116,637 gallons which in barrels is 1,917,590.

MR. COTTLE: I have a figure of 1,937,618 barrels.

MR. MCGRATH: I have 1,917,000.

MR. COTTLE: Yes, that is right, 1,917,000.

A The 590 is wrong. I did this in long hand the other night and it ought to be right.

MR. MCGRATH: 12 barrels difference is all it is.

A I may have made a mistake. What do you get, 1,917,000?

MR. COTTLE: 618.

A There is 28 barrels difference. You check that. Is that right? 618?

MR. COTTLE: 618 is right yes.

A Thank you. And the total cost of that quantity after adjusting for the inventory values is $2,914,005.02 which represents the cost of this quantity of material. Now you will note that this quantity of material 67,116,637 gallons is the same quantity as is shown as the sum of the next to the last column at the top of the page under the head "Net realization from crude and absorption naphtha." The total crude and absorption naphtha in that column is 67,116,637 gallons, so we now have accounted for all of the material produced during the year 1938. Then if we subtract the $2,941,005.00 from the net realization of $4,299,229.00, we find that we have a spread between the cost of the raw materials used and the price obtained for the finished materials of $1,358,224,28 and that spread was obtained from the 1,917,618 barrels. So that the total spread per barrel under these conditions was obtained by dividing that $1,358,000.00 by the 67,000,000 gallons giving 70.83 cents per barrel.

Q MR. FRAWLEY: Right there I have some barrel figures that Mr. Cottle has worked out showing how that 70.83 was arrived at. It might be well to put them in the record, just the per barrel figure which results, the per barrel figure which results in the 70.83 and the realizations at $2.2420. Have you any way of checking that?

A Is that dollars?

[illegible]

[illegible]

[illegible]

aide to a [illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible] had been said [illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

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Q That is dollars realization. That is $4,299,229.30 divided by 67,116,637 gallons. And then convert it to barrels and it comes to $2.2420?

A I imagine that is right. I cannot check it very carefully right up here.

Q I thought perhaps if you were using the same figures he was using you might take that figure there so it might go into the record at that place.

A What did you get.

Q $2.2420.

A I checked it to 2.24.

Q The cost of crude which we have is $1.5337 and that is the figure of $2,941,005.02 divided by --

A Wait a minute, two million and what?

Q $2,941,000.

A Divided by what?

Q Divided by 67,116,637 gallons and converted to barrels.

MR. COMMISSIONER LIPSETT: Divided by what?

THE CHAIRMAN: If Mr. Cottle knows these figures and you want them on the record at this moment for a purpose let Mr. Cottle, who is still under oath, stand up and give them to us, don't you think that is better?

MR. FRAWLEY: Yes.

THE CHAIRMAN: Instead of bothering Dr. Brown with all these figures that Mr. Cottle has already made.

MR. FRAWLEY: As a matter of fact I think I can simplify it. We have a statement,

Mr. Cottle has prepared a statement which shows in just a slightly different form the same information as is contained on Page "308" (c). We propose then to file this as soon as it is copied, to file it as an Exhibit and that will get all these figures in. So perhaps there is no use in pursuing that. The figure there of $1.5337 works out to .7083 per barrel.

A That is another way of getting the same figure.

Q Yes.

THE CHAIRMAN: What did you say at the last?

MR. FRAWLEY: It is the same figure .7083 per barrel, the same figure that is here.

THE CHAIRMAN: What point are we making?

MR. FRAWLEY: Simply you have the figure as we have it to ascertain the per barrel realization and subtract from that so many dollars per barrel, the cost of the crude. All I want to do is to put on Mr. McGrath's Exhibit at this place these per barrel figures.

MR. NOLAN: It is all there in a different way.

MR. FRAWLEY: Yes, of course, it is all here.

THE CHAIRMAN: I understand, Mr. Frawley,

Q MR. FRAWLEY: Now then what next?

A The next items on the sheet here are manufacturing costs, set down on a barrel basis and the manufacturing cost as set out in Schedule "3" of Exhibit "280", which we

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went over the other day, shows a total manufacturing cost for the crude and naphtha processed by the Imperial for their own account of $935,566.59. Now that figure has to be reduced by $19,384.75 because it includes that item I have just mentioned, which is the processing cost charged by the other refinery processing the Ioco naphtha. The Ioco naphtha has been excluded as a product of the Calgary refinery because it is used as a blending stock and therefore, the manufacturing costs of the materials produced at Calgary and sold from the Calgary refinery must not include this $19,384.75. With this subtracted it leaves us $916,181.84 as the manufacturing cost at Calgary of all of this material which has been produced from the Turner Valley crude processed by the Imperial for their own account at Calgary.

(Go to Page 9097)

Q And that figure $916,181.84 is found on Exhibit "308-C"?

A Yes, that is the figure which is listed manufacturing costs on "308-C". From that must be subtracted the value of the bunker fuel oil which was obtained from processing British American crude. According to the contract with the British American Company 9% of the crude owned by the British American and processed for them by the Imperial was to be retained by Imperial as fuel oil to supply the fuel required for processing British American crude. And that fuel in turn was included in the fuel oil sold by the Imperial Refinery at Calgary, but did not come from the Imperial's own crude. And this item in red "Less Fuel Cost," that should read, if it does not, "Less Fuel Cost" British American Processing $41,639.72, and that leaves us a balance of $874,542.12, being the manufacturing costs for the refinery in producing this quantity of finished products as shown on Exhibit "308-C". And that item $874,542.12 divided by the total amount of 1,917,618 barrels, gives 45.61 cents as the manufacturing cost per barrel of crude oil, crude naphtha and absorption naphtha as processed at Calgary. Now the next three items are the ones that perhaps we are most interested in for the immediate present. That is the difference between the total spread. That is the amount received for the finished product less the cost of the raw materials $1,358,224.28, and the manufacturing cost to convert these raw materials into the finished products, $874,542.12, gives a profit before Income Tax of $483,682.16, which is the equivalent to 25.22 cents per

barrel. Less Income Tax of $106,410.08, which corresponds to 5.55 cents per barrel, leaves a net profit after Income Tax of $377,272.08, which is the equivalent to 19.67 cents per barrel. Now if we then go to Exhibit "311" which shows the present capital investment, or rather as of January 1, 1939, and based on the depreciated value of the plant which appears to be the consistently depreciated value in view of their operating expense, we find in Exhibit "311" that the capital employed or the working capital on December 31st, 1938, was $2,976,032.01. And on that capital was earned this net profit after Income Tax of $377,272.08 which is approximately 12-2/3%. That really completes the analysis of the operation of the present Imperial refinery, based on present prices and on the throughput and production as of 1938. The Exhibits that I passed over, Exhibit "309" is one which I think should be ignored. It was prepared to show what the spread would be....

Q What is "309"?

A This is "309", it is another exhibit which I think should be ignored. It shows the spread based on the assumption, which is contrary to fact, that the material in storage on January 1, 1938, and on January 1, 1939, represented finished materials rather than materials in a semi-finished condition. It shows a difference of about 3 cents spread per barrel, which is not the true picture and which does not represent the facts.

MR. McGRATH: It is highly theoretical. At the time I handed in that I mentioned Exhibit "309"

was theoretical or hypothetical.

A You do not feel it should be considered do you?

MR. McGRATH: No, I do not think it should be.

A I think we are in mutual agreement on that basis that it should not be considered.

MR. McGRATH: That is correct.

A We have already discussed Exhibit "310" as showing the cost per barrel as a function of all the materials processed and I checked the figure on there for about 1,200,000 barrels I believe. Is that right, and found it to be 59 cents based on the market and operation of 1938. I put that on the record the other day. But I thought I would mention it at this time. Yes, based on the operation of 1938, but making an allowance or assuming a condition rather that the Imperial Oil Company was processing its own crude only, and was not processing the 781,233 barrels of British American, the cost per barrel would have been approximately 59 cents instead of the 45.6 as shown in this previous exhibit. And that is in very close agreement with the figures shown for 1937 in which case the barrels run were some 700,000 less than in 1938, and the cost shown is some 16 cents higher. So that I believe that Exhibit "310", which again is based on fact and past experience, is applicable with a fair degree of precision, to present conditions as indicating the cost per barrel for the different quantities of material run through that refinery. I believe that is all.

Q Yes, I think that is all on that.

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THE CHAIRMAN: We won't start a new phase. I have just been wondering, Mr.Frawley, if we should have the benefit of Counsel's ideas of what is meant, as to what would be the proper interpretation to put upon the words "fair and equitable." I mean take this situation. Let us take it as established for the purposes of the present discussion that every cent that is claimed was put into the capital expenditure by the Imperial Company. They certainly could be heard to say, whether or not other considerations would overbear it, that anything less than a fair profit on that particular sum, regardless of what consequences followed, was not fair and equitable. Equally I can conceive of someone saying "Well I do not care at all what the Imperial has invested in the light of the competitive situation now existing, that a different price is fair and equitable." Another person might say "Well, if they only had an efficient plant, the fair and equitable price would be so and so, and the public should not have to pay anything more." And that might be quite right, or it might be quite wrong. But I am getting bothered, I confess, about what we are to find in the end; to make a proper answer to that which we are commissioned to answer. It is giving me concern. I suppose we should have Counsel give that thought. We may be a long way away from making answers, but if we do not know in the end precisely to what our answer must be directed we won't be very intelligently appreciating the evidence as we go along.

MR. FRAWLEY: No. Well......

[illegible]

THE CHAIRMAN: I mean supposing we were told in this Commission in express words that the person we are concerned with is the consumer, that is concrete. You know. Or if the only person we are concerned with is the refiner that we are concerned with rather in determining these prices or it is the producer, or is it to be a conglomerate of the moral and economic considerations affecting all three? Is it a social problem? Is it an economic one? I am speaking now on the very broad aspect that some day we are going to answer.

MR. FRAWLEY: Yes.

THE CHAIRMAN: I can conceive perhaps Counsel will say to us at that time "Well you can only do your best to strike an average of fairness." Or Counsel may argue that you are only concerned with the ultimate consumer. I cannot conceive of the refiner saying something is fair which is less than fair, having regard to what they have taken out of their pockets.

MR. FRAWLEY: Yes.

THE CHAIRMAN: Even as our answer must have relation to such consideration, should not we have some idea now, if we can get one, of what is the right thing to do in the circumstances, in making answer, because it may have an effect on the evidence led.

MR. FRAWLEY: Yes. Now if you want some consideration.....

THE CHAIRMAN: Or it may not. I am just leaving it with Counsel in the hope of getting the assistance that we always get from them, to think

over.

MR. FRAWLEY: Yes.

THE CHAIRMAN: I confess it is bothering me.

MR. FRAWLEY: I will give some thought to it and speak to the Commission again about it. I am sure Mr. Nolan will do so too. Perhaps I may make this observation in passing, of course the Commission must be read as a whole. All of the Commission must be read together. While we find you are asked to find the fair and equitable cost of refining and the fair and equitable refinery door price, still there are these other clauses in the Commission which direct you to consider - whether or not with regard to the production, processing, handling and gathering, or distributing of crude petroleum and refined petroleum products in the Province, whether there is any expenditure incurred in or incidentally to these things which either wholly or partially is unnecessary, or not essential or not in the public interest. That is some guide in bringing us to what a true and proper meaning of that expression "fair and equitable price and fair and equitable costs", should be. I think we can speak to it more fully.

THE CHAIRMAN: I do not know, one could think that perhaps - well I do not know what to think. We are facing realities. We know that His Honour's Commission was probably inspired with a Government who probably would be concerned with the good of their people. Now, then where does that lead, where there may be a conflict between classes?

That is to say supposing the consumer could only get a fair price for gasoline if the man who produces the gasoline must sell it at less than its actual cost to him to do it.

MR. FRAWLEY: Yes, is that fair and equitable?

THE CHAIRMAN: Yes. I am not pressing for any argument tomorrow or any time. But I want to put it before Counsel that we are finding it bothersome, and if they can give assistance we will be glad to have it.

(At this stage the Hearing was adjourned until 10.30 A.M., June 16th, 1939).

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The Province of Alberta

IN THE MATTER OF THE PUBLIC INQUIRIES ACT

—and—

IN THE MATTER OF a Commission, dated the 12th day of October, A.D. 1938, to inquire into matters connected with Petroleum and Petroleum Products

Commissioners:

The Honourable MR. JUSTICE McGILLIVRAY (*Chairman*)

—and—

L. R. LIPSETT, ESQ.

Session:

Friday

CALGARY, Alberta JUNE 16th, 1939

VOLUME 79

differentials
spread fair 9202

Blum

1957 – Lake the lowest cost refiner as controlling factor in pricing prices

I N D E X

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DR. G.G.BROWN, having been recalled, examined by Mr. Frawley said:

Q Now Dr. Brown, we had completed a discussion of the Exhibit "308", (A), (B), and (C), and I had intended to ask you something with respect to this figure----

THE CHAIRMAN: Mr. Frawley, had the witness completed "308" (C) before I interrupted him, I do not just remember but I thought he had not, had you Doctor?

A Yes, I had carried that through to the net profit shown there at the bottom of the page, $377,000 and then referred that back to the invested capital at the end of the year, which is Exhibit "311", and indicated that it would show a return on the invested capital of about 12-2/3 per cent.

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THE CHAIRMAN: Yes, I remember that, All right.

Q MR. FRAWLEY: Now I had intended to ask you something about the 1938 realizations of gasoline, namely, 9.1 cent per gallon, and to ask you if it were possible for you to tell us what the cost, by the way that realization of 9.1 cent as I understand it is a composite figure which indicates what the company got back from all the jobbers and at all the prices charged the jobbers?

A For all three grades of gasoline.

Q For all three grades of gasoline?

A Yes.

Q Now we know and it is clear from the evidence, perhaps you have not been paying much attention to it, that the companies pay, and you would expect that to be so, that the companies pay something more, the jobbers pay something more for a tank car of Ethyl Gasoline than for a tank car of Standard Gasoline and something less than either of those figures for a tank car

of third structure gasoline, that is an obvious situation is it not?

A That is right.

Q Now the company charges different prices and that is something which we will discuss, and you would expect us to discuss, when we get to marketing, that is true, is it not?

A That is right.

Q Nevertheless it has occurred to me that we might at least ask you to tell us why, if it be impossible, it is impossible for you to tell us what it costs the company to make that car of Ethyl Gasoline which they sell to jobbers and what it costs them to make a car of gasoline which they sell, of Three Star which they sell to jobbers and a car of Acto and distillate and so on, and I thought that perhaps one way of you to approach that would be to give the Commission a description of what the refining operation is in some detail and perhaps in doing that you might work into this question of the impossibility of finding the cost of each kind of gasoline?

A Well you would like to have me begin with a description of the processes followed in refining crude oil.

Q In refining crude oil and chiefly confining yourself to the Alberta operation with which the Commission is chiefly interested and as we go along explaining those terms which from time to time the Commissioners have heard and with respect to which they cannot be expected to have any particular knowledge?

A Well the crude oil is the material which is produced from the ground in liquid form and exists in the ground as liquid. Then there is some material called "crude naphtha" which is a condensate from the gas which is produced from the oil and gas horizon. The crude naphtha has to be processed at very much the same way as the crude oil in the sense that it has to be distilled and treated, so that I think for simplicity's sake we

ought to consider that the crude oil and the crude naphtha are perhaps treated in the same manner at the refinery, that is a simplification but I think it is justified. Then there is the absorption naptha which is a material absorbed out of the gas by an absorption process and recovered from the absorption oil in which it has been absorbed from the gas. It has a high vapour pressure, a very volatile product and in order to use it efficiently in blending with motor fuels it is necessary to stabilize it, that is to remove these extremely volatile constituents which would cause it to vapourize too readily. If you take the raw absorption naphtha and blend an appreciable amount of that with gasoline the very volatile constituent in the absorpition naphtha will vapourize, that is in the fuel lines of the car, so that the fuel pump which is pumping the gasoline from the tank at the back of the car, at the rear of the car, up to the engine, will have to handle a relatively large quantity of vapour, that vapour being given off due to the vapourization of these extremely volatile constituents and under such conditions the capacity of the pump on the engine is not sufficient to handle this large vaporized volume and at the same time to supply enough liquid fuel to keep the engine running and that is known as "vapour lock", which is a difficulty which has been very widely experienced and has to be overcome if the car is to operate in a satisfactory manner. Therefore this absorption naphtha is treated in the refinery by a process known as stablization which removes these very volatile constituents and reduces the vapour pressure of the absorption naphtha to , I believe, somewhere around 10 or 15 pounds before blending, do you know what that is?

MR. McGRATH: No I do not know what that is.

WITNESS: Anyway the vapour pressure is reduced to a safe limit. Vapour pressure is a term which is expressed in the units of pressure such as pounds per square inch and represents the tendency of the absorption naphtha or other material to form vapour. If we have the absorption naphtha at 100 degrees Fahrenheit and find that we have to keep a pressure on the absorption naphtha of 27 pounds per square inch in order to prevent it vapourizing, we then say that the absorption naphtha has a vapour pressure of 27 pounds, so that the absorption naphtha has to be processed to a certain extent at the refinery but ordinarily that operation is not considered as part of the refining operation of crude oil although the expense must be borne by the refining operation.

Now to go back to the crude oil and naphtha which we will treat together for the sake of simplicity, the crude oil when it is brought into the refining area is run into tanks for temporary storage. From those tanks the crude oil is pumped through heat-exchangers, which heats the crude oil on the way to the stills by heat-exchange from the hot oil leaving the still. It is a measure for economizing fuel and increasing generally the efficiency of the operation. After the crude oil has been heated to perhaps 250 degrees Fahrenheit it is then usually passed through a settling tank under preassure and at this temperature in order to settle out of the crude oil water and sediment which might cause trouble in the refining operation, in other words clean up the crude oil. This oil then at a temperature of about 250 degrees usually then goes to the still. Now these stills may be of various types of construction. In the modern plant, those which have been built in the last few years, it is al-

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most always a pipe-still in which the crude oil passes through a pipe, a steel pipe, of about 3½ or 4 inches diameter in a furnace and in passing through this pipe it may be heated to a temperature of some 600 or 700 degrees Fahrenheit and a large part of it vapourized. Then the mixture of vapour and liquid leaving this pipe still will be introduced into a fractionating tower or bubble tower which consists of a tower perhaps six or eight feet in diameter, depending upon the size of the plant, and from 40 feet up to perhaps 80 feet or more in height. This tower consists of a number of trays or bubble trays, as they are called, which contain or hold pools of liquid and the vapours passing up from below is forced to bubble through these trays of liquid on its way to the top of the tower. At the top of the tower the vapour is condensed, part of it removed to form the liquid products such as the crude gasoline or raw gasoline and part of it returned to the tower to supply these pools of liquid which are formed on each one of these various plates. As the vapour passes up through the tower and comes into contact with these pools of liquid, there is an exchange of material, the more volatile material in the liquid pool is vapourized from the liquid and passes up the tower with the vapour, while the less volatile materials in the vapour are condensated out of the vapour and absorbed in the liquid pools on the various plates. This action consists essentially of a number of successive distillations and condensations. The temperature of the vapour and liquid as it is introduced near the bottom of the tower from the pipe still may be 600 or 700 degrees and the temperature of the liquid and the vapour at the top of the tower may be about 300 to 350 degrees, so that only

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those constituents which may exist in the vapour state at atmospheric pressure, at about 300 Or 350 degrees will be carried overhead from the top of the tower as a vapour and that stream constitutes the raw or crude gasoline. Somewhere down this tower, perhaps 6 or 8 plates from the top, the liquid, in one of these pools, will have such properties as would be desirable as a burning oil such as kerosene, or possibly a furance oil or such product as desired. For that reason some of the liquid which collects in this pool, say 6 or 8 plates below the top, is removed as a side stream. The stream of vapour removed from the top would be called an "overhead product" or "top stream" and this stream of liquid removed part way down the column is referred to as a "side-stream" because it is removed from the side of the tower rather than the top and out of that side stream liquid which is removed would be produced the kerosene and other types of burning oil.

Now at the very bottom of the tower will collect those high boiling fractions which are not vapourized by the heat supplied in the pipe still and also those high boiling fractions which are removed from the vapours as they pass upward through the successive pools of liquids and this bottom product is frequently referred to as "fuel oil" or "the residue" or "residuum". It is a residue in the sense that it is the residue left behind through the distillation operation. This residue is then usually, in a modern plant at least, sent to a cracking still which is constructed in very much the same general way as the still I have outlined except that it operates at higher temperatures and higher pressures, and it has other devices in the plant for special functions, but it is generally similar, so that

residual product removed from the bottom of this fractionating tower, would then be treated at a temperature from 900 degrees upward, usually in a pipe still of somewhat similar design, and then frequently passes through what is known as a soaking chamber or reaction chamber which is simply a large vessel perhaps 40 feet high and 10 or 15 feet in diameter which is built to stand high temperatures and high pressures, so that the oil, this residual fuel oil, after being heated to a temperature of 900 degrees of more, is then flowed into this reaction chamber at such a rate that it may stay in that reaction chamber a matter of 20 to 40 minutes more or less, during which time the cracking operation which was started in the furnace, due to the high temperature of the oil in the furnace, continues, and the cracking operation is then allowed to continue to produce the desired product from this residual product of the topping or first distillation unit. The vapours from these reaction chambers will then pass up to a similar bubble tower or fractionating tower, with the overhead products removed, which will constitute the crude cracked gasoline. In some cases a side stream might be removed also from this plant for the purposes of producing a structure distillate or for other burning oils but usually not kerosene and the very high boiling fractions which do not vapourize and will be taken out from the bottom of this tower by some similar equipment, is then a cracked residue. It has a very low gravity and a low viscosity but is not usually useful for any purpose except commerical heating where the equipment is designed for handling such heavy fuel oil and in some cases it may be converted into road oil for putting on the road or a synthetic asphalt and in some operations it is

cracked considerably further and produces coke.

Now in these operations we have essentially two units, there is the first unit of the furnace and tower, which is called a topping unit for the reason that it tops out of the crude oil the more volatile components such as those which would constitute gasoline, tractor distillate, kerosene, light fuel oil and similar materials and leaves behind a residue but all of the material removed from the tower in this topping plant was origianlly present in the crude oil but it was present in the crude oil as a more or less homogeneous solution and tho gasoline has to be separated from the crude oil by the operation known as "topping", in much the same way as you might say the cream and the skim milk are the two components of ordinary milk but we cannot separate these unless we put this milk through a process such as a separator and in putting it through the separator we get the two streams , cream and the skim milk, each of which was present in the milk as it was originally supplied to the separator. There is no chemical change brought about in this topping plant and the products from the topping plant are referred to as "straight run", such as "straight run gasoline", being the gasoline produced from the topping operation, meaning any cracking or straight run kerosene and so on.

Cracking

Now these products which are produced from the cracking unit which operate as a residue from the topping unit are all products which have been produced by some chemical change brought about by the cracking operation. There was no gasoline in the heavy residual fuel oil which was supplied to the cracking unit. Whatever gasoline has been produced from the cracking unit has been produced by inducing a chemical change in the material supplied to the cracking unit. So that all of these products are in their true sense synthetic. The cost of the cracking operation is always considerably greater than the cost of the topping operation because of the increased cost in the equipment necessary to withstand high temperatures and pressures and the longer time required to carry on these chemical reactions and a very, very important consideration is the fact that in these chemical changes there has been produced a rather large quantity of gas which is useless except as fuel in the refinery, or if there happens to be a good market for gaseous fuel it might be sold as gas. This gas and some of the coke which is formed constitutes a loss in the liquid recovery from the cracking operation and a good part of the loss shown in these figures we have been discussing is due to this loss incurred in the cracking operation. Carrying it, therefore, to this point, we have simply the crude or raw streams from which the finished products will be made by chemical treatment and by blending. For example the crude or raw gasoline stream taken from the top of the topping tower must be treated to

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remove the mercaptans and other sulphur materials, or at least convert the mercaptans into other sulphur compounds. In the Mid-Continent fields of the United States the quantity of mercaptans in the gasoline is reasonably small and it is simply necessary to convert this evil smelling mercaptan compound into other sulphur compounds by a process known as sweetening, which does not remove any sulphur but simply sweetens the gasoline so far as its odor is concerned. In the Turner Valley crude the mercaptan content is so high that it is necessary not only to convert the evil smelling mercaptan into other sulphur compounds which have a different odor but it is also necessary to actually remove some of this sulphur which may be present as mercaptans. So that in treating this crude of Turner Valley here in Calgary the Imperial have evolved a method which seems to be very successful and economical in reducing the sulphur in the gasoline that may be present as mercaptans. So that this raw gasoline stream removed from the top of the topping tower is then processed again by putting it through another furnace and bringing it up into a vapor condition, to perhaps 500 degrees more or less and passing it through the towers under about 30 or 40 pounds pressure in which there is alumina which is a mineral having a more or less catalytic action on these gasoline vapors, and this alumina converts the mercaptans into other compounds such as free sulphur in the form of hydrogen sulphide. Now the hydrogen sulphide can be removed from the gasoline by treating it with some alkali wash. So by putting in this

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special treating process of the Bauxite treater it is then possible to produce a gasoline of sufficiently low sulphur content and of a satisfactory odor from this Turner Valley crude where it would be extremely expensive to produce a satisfactory product insofar as the sulphur is concerned by the ordinary methods such as are used in treating crudes which do not contain so much mercaptans. That is one of the operations which has to be undergone in order to handle Turner Valley crude in a satisfactory manner and is one of those things which increases the cost of the operation of Turner Valley crude as compared with other crudes which are not cursed with so much mercaptan sulphur. Well, similar but different -- I mean equivalent but different treating operations are also given to the side stream which will compose the kerosene and other products that may be removed from the topping operation. Now go over to the cracking unit. We find that the gasoline, the raw gasoline from the top of the cracking unit must also be further treated. There are different ways of doing that. In the Imperial plant as it is now operated, this stream is given a treatment with clay and rerun in another distillation unit to produce a clear colored and stable gasoline which will not form gum in use and not cause trouble due to sticking valves, which is a thing we discussed the other day you remember as part of the problem that had to be met by the technical service division. And in re-running or redistilling this cracked gasoline there is left behind a residue which may be called

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P. D. Bottoms P. D. being the abbreviation for pressure distillate. The term "pressure distillate" being applied to cracked gasoline as distinct from the straight run or topped gasoline. The term "pressure distillate" was introduced because this cracked gasoline was produced under pressure and it was a distillate product. The product taken off was not suitable for gasoline so it is called pressure ditillate. Then this pressure distillate being re-distilled leaves behind a residue which has been called pressure distillate bottoms, or in the short-hand of the industry P. D. Bottoms. And these pressure distillate bottoms may then be blended with other streams to constitute part of the tractor fuel. And then finally the cracked fuel oil which is dark or black colored material and appears dirty to look at but it may be a reasonably clean product in the sense it does not contain much solid carbon, is then sold as an industrial fuel or possibly used by the railroads or something of that kind. Or it can be used as a material that can be reduced to synthetic asphalt or road oil depending upon conditions. Now you can see that there are so many varied products or streams produced from this one raw material, crude oil, that the cost of producing any one of these streams can be determined only after we have fixed an arbitrary cost for all of the other streams. If we take a simple case such as the dairy farmer who produces milk. It is possible perhaps by a system of accounting to determine over a period of years how much it costs that dairy farmer to produce one gallon

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of milk, but if you ask him to determine what his cost of producing one gallon of cream is as distinct from the cost of producing one gallon of skimmed milk, you can appreciate the difficulty he would have. Because the cream and the skimmed milk are the two components which make up the natural milk and he cannot fix the cost for producing his skimmed milk unless by some basis the cost of producing the cream is first arbitrarily fixed. In other words, if there is a good market for cream he can put all his cost of production on the cream and then the cost of production of the skimmed milk would be zero. Or it may be the case that the cream brought a very fancy price and his cost of producing milk would be less than zero and he would be justified in pouring the skimmed milk on the ground and selling only the cream rather than selling the milk because he may then actually make more money. The same condition exactly applies in the effort to determine separately the cost of the various products that are produced from the refinery. If there is an excellent market for gasoline and kerosene and no market at all for the heavy fuel oil, as actually exists at times, the refiner would be justified in producing all the gasoline and kerosene that he could and saying that the entire cost of production must be borne by the gasoline and the kerosene. He takes the fuel oil and burns it in a pit as a waste product. On the other hand if we can affix the cost of production, if there be such a thing, of the fuel oil and of the tractor distillate and of the kerosene and of all of the other products that may be produced from crude oil, except one, then

by the difference we can arrive at the cost of producing that one product. So that I believe that it is utterly futile to regard a refining operation from the standpoint of trying to determine the cost of producing any one of the particular products that may be produced. However, if we take all of the products which are produced from the crude oil we can then determine the cost of producing all of those products, because we know the total cost of processing the crude oil and we know that all of the products produced from the crude oil were produced at that cost. So that the only satisfactory way of arriving at the cost of a refining operation to determine the capital return and whether things are as they should be, is really to consider the cost of processing crude oil to make the products which were sold and to consider on the other hand the total return from all of the products produced from the crude oil. So that for that reason in discussing the return from the sale of gasoline we have included in that one item all of the returns from all of the various grades of gasoline sold to the jobbers. Even if it was desirable for some other purpose to try to arrive at a figure for the return to the refinery for Ethyl gasoline as distinct from their regular brand and for the third structure as distinct from their regular brand, which would be an extremely difficult thing to do because I doubt if the records are kept in such shape that we even could do that, but if an attempt were made to do that, we would immediately put them all together again and come out with an average figure such as this 9.1 ¢.

[illegible]

per gallon such as in Exhibit "308" (c). So that we have a number of these items separated and our effort is to put them all together and come down here at the end to a figure of 70.83 cents per barrel for the spread between the cost of the barrel of crude oil and the price received for all of the products produced from that barrel of crude oil.

Q MR. FRAWLEY: In other words, to find what a refinery is doing. making money or losing money, and if so how much, you have not got to know how much they get for their fuel and how much they get for their oil, except as a means to an end?

A That is right. What you know is how much they get for all of the products.

Q From the crude oil?

A Right.

Q THE CHAIRMAN: As I understand they then can arbitrarily put their cost where they will with respect to all products?

A Except one.

Q Yes, except one?

A Except one. In other words, the cost of treating or processing a barrel of crude oil can be determined and that was determined for the conditions as set forth in Exhibit "308", and reported in "308" C as 45.61 cents per barrel. Now the cost of producing all of the products from one barrel of crude oil must total 45.61 cents?

Q Yes?

A Therefore you can arbitrarily fix the cost of producing

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all the products except one and then by the difference that one must make up the 45.61 cents. And that one may have a negative cost or an exorbitantly high cost, depending on how the others are fixed which is a purely arbitrary manner. The only consistent way to look at it is the cost of producing all of these products which were produced from a barrel of crude oil was 45.61 cents, and the returns from the sale of all of these products should bear a proper relationship to the cost of producing all of those products. That is to say the cost of producing that I have given you, 45.61, is the cost of processing in the refinery. It does not include the raw materials cost.

Q Now a customer who wants gasoline we will say, a motor car fuel, is very much interested in where those costs are to be, isn't he? He does not care a bit what the other products cost?

A That is right.

Q So all these refineries may decide where they will put their costs, and of course if they do that with regard to everything, they have to leave one over because it picks up the slack. But they nonethe less as I understand it, and perhaps of necessity, but I want to understand it, they put their cost against whatever product they like and there is no way of showing that is unreasonable or improper?

A Perhaps I have given you a little wrong impression in saying we can put an arbitrary cost against all products except one. That is simply a way you might do it on paper. In actual practice the refiner

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does not put his cost against any one of these. He simply sells all of them for what he can get for them and then adds up what he gets for all of the products he sells and figures whether he is making money or losing money. If he is losing money he says "I have to get something more for some of these products", and he works around and sees what he can get for them. In other words, the selling price although it is influenced by the refiner, is actually determined in the long run by supply and demand and other economic factors.

Q That is tho sales realization theory, I suppose?

MR. FRAWLEY: Yes.

Q THE CHAIRMAN: Cost is related to the price you get?

A Cost is related? No. I do not think so. The cost of processing one barrel of crude under these conditions was 45.61 cents, and the cost of the crude oil and other materials, the absorption naphtha, averaged about $1.42, something like that. So that the cost of producing all of these materials by the refiner is a definite figure, which is about $1.90.

MR. COTTLE: $1.99 crude plus refining.

A Yes, the crude and the absorption naphtha and the other things average around $1.99. So the cost of producing all the products produced at the refinery is a definite figure of $1.99 per barrel. Now that is fixed. That is definite. Now, the return from the sale of those things must equal $1,99 if the refiner is to break even.

Q THE CHAIRMAN: Yes?

A But the return is not the cost. The cost is $1.99. The return may be $1.79 or it might be $2.19.

Q MR. COTTLE: In this case it is $2.24, Dr. Brown?

A In this case the return is $2.24 against a cost of $1.99.

Q THE CHAIRMAN: That is on all products?

A On all products. I cannot see how that $1.99 is in any way determined by the $2.24. I think that is what you indicated, Mr. Frawley, wasn't it?

Q MR. FRAWLEY: Yes.

A I do not see any relationship between these two. $1.99 is a definite figure arrived at by the cost of crude and the cost of processing.

Q THE CHAIRMAN: Yes. But that is all very well, and I think I understand it. But one is impelled to the conclusion from what you say, it is quite impossible to say whether or not a person buying only gasoline is paying the proper price?

A You must again say a proper price on what basis.

Q Quite so. That is one of our worries, of course.

A That is the whole thing.

Q If we cannot find out what it costs to make a barrel of gasoline it would appear that we are somewhat in the dark as to what is a fair price for a barrel of gasoline, outside of the well known basis of whatever the traffic will bear. As I understand you, the refinery practice - and I am not criticising it, but I want to understand it?

A Right.

Q As I understand you, in all refinery practice you get

so much crude and you sell for what you can all your products?

A Yes, that is right.

Q You know what it has cost you to refine that barrel of crude into the various products that you have. You know what you have gotten for all of those products, but it is impossible to say as to what the precise cost has been in respect of any product, any one.

A Any one alone?

Q Any one alone. Yes, quite so?

A That is right.

Q It may seem perfectly absurd to all refiners or to anyone representing them, but the fact is we are asked a question which would imply that we should make answers about this, and if we cannot our task is insurmountable. If we can, I want to know how?

A It seems to me the only way to do it would be exactly the same way you would approach the problem of what is a fair price for cream. If you know the price for milk, if you have determined a fair price for a gallon of milk, what is the fair price for a gallon of cream? You are faced with exactly the same dilemma. In order to determine the fair price for cream, you have to determine the fair price, arbitrarily or by some other means, for the skimmed milk.

Q MR. FRAWLEY: And you say it is just as impossible to find the cost of fuel oil as against all gasolines. It is not only impossible to find out the cost of the various kinds of gasoline, but it is just as impossible to find out the cost of all of the gasolines as against all the other fuel oil?

A Yes.

Q Suppose you were just making two things, gasolines and furnace oil, we will say, some other particular product. Just two markets instead of many, and all of your crude oil went into two barrels; gasoline, which you afterwards separated and classified and marketed and this fuel oil which would be used as burning oil, we will say, in furnaces and so on. You say there again you cannot say these gasolines cost you so much as distinguished from the fuel oil. That is so is it not?

A You cannot determine the cost of one unless you have the cost of the other.

Q It is an endless chain?

A There are as many variables as there are products produced, and there is only one equation, and to solve one equation you can only have one unknown. So all the variables must be known but one.

Q THE CHAIRMAN: Because in the process of making them all - or rather the processes by which they are all made are intermixed and entwined as it were?

A Yes.

Q That is the reason. You do not go along to a certain stage and drop there one product and move along further and get more and so on?

A No.

MR. FRAWLEY: You pick them up and bring them back and re-run them?

THE CHAIRMAN: I understand. Your explanation this morning has been very helpful. I

understand it.

Q MR. COMMISSIONER LIPSETT: Is your cost of crude taken at $1.30 plus 15 cents pipe line rate?

A The cost of crude shown in this exhibit "308-C", which is now a matter of history representing the 1938 operations, is shown for Turner Valley at an average of $1.37-7/10 cents per barrel.

Q Does that include the 15 cents pipe line freight?

A Yes, it included the cost of the crude laid down at the refinery. Right in here. These are the costs of the other materials.

Q There was just one other question, Dr. Brown, I would like to be shown. I think perhaps we have it. What is the percentage of loss between the original barrellage of crude oil that goes into the refinery and the total products recovered from the barrel?

A In gallons you will find - I will give you the percentage and I will show you how I get it. In gallons it is shown in the next to the last column, 4,000,000 gallons loss out of a total of 69,000,000. It is 4,158,000 gallons divided by the 69,032,000, which is about.......

Q MR. COTTLE: Is that right? I think it should be divided by the 67,000,000 gallons because the production of 62,958,000 comes from the 67,116,000 after adjusting by the unfinished stocks.

MR. McGRATH: The 1,917,000 unfinished stocks is production from that crude, Mr.Cottle.

A Yes. That was not sold. The 1,915,760 was not sold but it was produced from the crude along with the loss of 4,158,000. I think that is right. So 4,158,000

divided by the 69,032,000 is just about 6%. So the loss in the over-all refining is about 6%. Now that loss is composed not only of the loss experienced in the cracking operation, but also the loss in the treating operation as we remove the mercaptan, sulphur and other materials from the various products, there is certain loss in that chemical treatment and that is also included.

Q THE CHAIRMAN: Do I understand that in - I suppose you have not made any examination of the accounts, and perhaps Mr. McGrath will tell us. These are not severed in the books at all. This cost of making anything, no attempt has been made to sever......

MR. McGRATH: In our books? No sir.

THE CHAIRMAN: It is the total?

MR. McGRATH: That is so. That is the way we look at the picture. There may be statistical statements made up, but this is the true picture of affairs right here. That is the way we look at it.

THE CHAIRMAN: How do you arrive at what you put as the cost price opposite a barrel of gasoline, and the cost against a barrel of some other fuel that we have been led to think is a cheaper kind? Namely, some other distillate, farmers' distillate?

MR. McGRATH: Costing the same?

THE CHAIRMAN: Yes. It costs less than Esso, I suppose. I mean costs less for the jobber to buy.

MR. FRAWLEY: Why do you say that a barrel of heavy fuel oil for tractors costs less than a barrel of Esso? That is a good question to bring this thing up.

MR. McGRATH: We do not say. We say we make a certain return on a barrel of crude and that is the proper way to look at it, just as Dr. Brown has explained.

MR. FRAWLEY: Now you do say, it is S. R., I think?

A Let me cover that.

THE CHAIRMAN: Excuse me, Dr. Brown, for interrupting all the time, but we hope to understand all this.

MR. McGRATH: We have a situation in inventories when we finish the end of the year. We have an inventory of gasolines, refined oil, tractor distillate and fuel oil out of proportion, probably, to the production of crude. It is necessary to place a value, some sort of a value, an arbitrary value on these products. Now, the way we determine that - mind you this is arbitrary, but it is consistent.

THE CHAIRMAN: I am getting to understand that perfectly.

MR. McGRATH: We take a barrel of crude, plus the manufacturing and that is the total cost of running the crude oil.

We know the fields which we get from them, from that barrel of crude.

Q THE CHAIRMAN: Yes?

A We price the yields which we get from the barrel of crude at the selling prices,then we take the total cost of the crude oil and manufacturing and proportionate it over the products on the basis of the volume and the selling price.

Q Yes?

A It is an arbitrary method.

Q I understand that?

A And that has been done for years.

Q Now, what I am getting at, going behind that, how do you decide to fix the selling price, I understand that you can allocate your cost with relation to what you have got?

A Yes.

Q But how do you decide what to ask?

A Well...........

Q Why do you not ask a lot more for farmers' engine oil than you do for Esso?

A That is a Selling Department matter, we are here producing products.

Q That is Mr. Halverson?

A I think so. Anything dealing with marketing is Mr. Halverson, and we are dealing with refining at the present time.

Q You do not fix the price for your Marketing Department?

A We do not, for the simple reason, if we did the accounting involved is tremendous. Some years ago we had billing prices and it consisted of 1,700 prices across Canada and it meant we had a staff working on billing prices all the time which could have been used for some other useful purpose

and it was gaining nothing and we had a great reduction..........

Q Somebody in your organization, and you think Mr. Halverson, will be able to tell us why it is that you charge more for Esso gaoline than for tractor distillate?

A I imagine he will explain the competitive situation on that, and I think that is the way he will cover it.

Q MR. FRAWLEY: Then although he will probably have to say, almost have to say, that his Refining Department cannot tell him what the Esso costs any more than the tractor distillate?

A That is right. We are interested in whether we make money on a barrel of crude oil, or not, that is our primary purpose.

Q You just leave it all to the Marketing Department, they can charge more for the various products, the farmers' distillate?

A As Dr. Brown expressed it, it is on a competitive basis, and I do not think they will charge more.

Q But under extraordinary competitive conditions, the tractor distillate might be a much more valuable product than high octane gasoline, and Mr. Halverson might be justified in asking more for it?

A That tractor distillate, I do not know, it may be of more value.

Q More value, and a higher value than the octane gasoline?

A Why do you say that?

Q It is an assumption?

A Oh, it is an assumption?

Q Yes, I am suggesting it might very well be, you say he does not fix the prices because of cost, that is one thing clear?

J. McGrath

A Yes, that is correct, that is correct.

Q Then it is left entirely to competition?

A Yes, I would say that.

Q Cannot you imagine some extraordinary condition, some extraordinary condition in some extraordinary territory, where there were no automobiles at all but a lot of tractors, you see, and I quite agree it is an absurd assumption, but I want to put it to you that it goes that far, that the price which the Marketing Department, the price which they charge for these various products is according to the market demand, the marketing situation and competition, purely and simply, and not cost at all.

MR. NOLAN: If there were not automobiles we would not refine any gasoline.

MR. FRAWLEY: No.

Q MR. FRAWLEY: I can give you one, take your Royalite coal oil in your own experience you had that at one time, there was more demand in your Imperial organization for Royalite coal oil than for high octane gasoline, that was the thing you were shooting for at one time?

A That is a long, long time ago, Mr. Frawley.

Q It is a long time ago, in the bush country in old Ontario?

A I am not that old.

Q I have read it, I think?

A I think so.

Q In some Imperial Oil Review?

A Yes, I guess so, but I cannot discuss selling prices because I do not know anything about them.

J. McGrath

Q MAJOR LIPSETT: Does that apply, also, Mr. McGrath, with regard to fixing prices for the jobbers, I understand for your own marketing organization you do not fix any prices, Mr.Halverson does that?

A Yes, the fefinery fixes no prices to anybody. They turn the gallonage over to the Sales Department and the Sales Department are the ones who establish the prices to jobbers and the tank-wagon prices. The refinery does not set any price of any of the products.

Q Is that set without regard to any question of cost of any oil, or do they get the average cost of the whole thing?

A I think the company or any company is primarily interested in the profits and the value on the crude of the entire operation, that is what the refinery is concerned about. Now arbitrary methods of distributing costs tell you nothing. This is the real, the true facts of the thing, whether you are making a profit on a barrel of crude or not.

Q THE CHAIRMAN: You say it is just a matter of, really a convenient way of dealing with it, and it is as good as any to say that which brings you in the most you charge the most expenses to?

A No sir, we do not charge the most expenses to.

Q But some other Department does, does it not?

A No, the only thing that I say on an inventory, if we have to figure an inventory then it is necessary to take a price for that purpose, because an inventory is not on the same ratio as the production of crude.

Q You do not charge at all?

A That is right, sir.

Q I understand that.

A That is right, sir.

THE CHAIRMAN: We will hear Mr. Halverson some day. We have heard a lot about him.

That is what I want to make clear........

MR. FRAWLEY: We will bring him in with pipes and drums when he comes.

WITNESS: I want to make myself clear on that. I have mentioned Mr. Halverson's name when it comes to selling, in the Sales end, and properly so, because I know nothing about it, so any questions you ask me about the sales part of our organization, I say "Mr. Halverson". I am not passing the buck.

THE CHAIRMAN: Oh, no.

MR. FRAWLEY: Oh no, but let me say this, this is a fair question, you do not really care, as a refiner , you do not really care what Mr. Halverson charges for the products a, b, or c?

A I think the Directors of this company are interested in what money they make in, from a barrel of crude.

Q That is really the nuts of it, you do not care what he charges?

A We have nothing to do with the selling end.

Q What he charges for product a, b, or c or d, it is what he brings back at the end of the year, and that is what you are interested in?

A Yes.

Q THE CHAIRMAN: And if you owned the crude, it would be a pure matter of selling crude, a pure matter of selling crude?

A I do not understand you, sir.

Q I say if you owned the crude?

A Yes.

Q All this business of refining it and marketing it and so on is disposed of and you are left with the disposing of your crude?

A Taking the barrel of crude out of the ground and with the refinery tools, converting it into products which were sold, if we owned the crude.

Q If you owned the crude?

A Yes, but unfortunately, we do not.

Q You are not entirely devoid of it?

A Well that, I should withdraw that remark, that was not a proper remark to make, and I will withdraw that, sir.

THE CHAIRMAN: That is all, thank you, Mr. McGrath. All right, Mr. Frawley.

Q (MR. FRAWLEY: To Dr. Brown): Now, I think that particular phase has been explored unless someone has some more questions while we are at that, and if there be any, I suggest they be asked now, because I am going on with Dr. Brown, on a different matter entirely.

THE CHAIRMAN: I would like to get this clear, you see when you put a competent expert in the box his evidence should be related to the things we have to answer.

MR. FRAWLEY: Yes, Of course he has not left the box, he is to come back.

THE CHAIRMAN: I understand that, but right here, here is a witness who ought to be competent to say "Your task is unsurmountable, you cannot get anywhere, you cannot possibly say this", if he knows that to be so, and if the questions and his answers

are not satisfactory in your view, we will see what other experts there are. I mean, we have concrete questions here, if we cannot tell the Lieutenant Governor of this Province that gasoline should be a certain price because we have no idea but what the distillate is distorted, and so on down the line, of all the refined products, all right.

Q MR. FRAWLEY: Well, Dr.Brown........

THE CHAIRMAN: If it is competition, then we had better be finding out about competition in this matter, insofar as competition affects us here.

MR. FRAWLEY: Competition in crude.

THE CHAIRMAN: If that is the sole determining thing to determine what is fair.

MR. FRAWLEY: Yes, well of course we have not..........

THE CHAIRMAN: I do not know, Mr. Frawley, I mean I am in the dark as you know, and I want to make it clear that a man competent to speak with respect to our concrete questions........

MR. FRAWLEY: Well, not all of them.

THE CHAIRMAN: Ere he is through, should answer those which are within his field if he can.

MR. FRAWLEY: Now, that is it.

THE CHAIRMAN: So that in the end we will be acting on and coming to conclusions on the advice of experts.

MR. FRAWLEY; Yes, that is quite so.

THE CHAIRMAN: So far as it is proper.

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Dr.G.G.Brown

MR. FRAWLEY: We do not want to take Dr. Brown out of his own department, but let us see if we can explore it any further, and perhaps we have explored it as far as we can. Now, Dr. Brown, one of the things which the Commission must go into under its commission, is,,they must conduct an inquiry into and to make answers with respect to, amongst other things, with respect to the fair and equitable price, maximum and/or minimum, which should be charged by wholesale and by retail for refined petroleum products in the Provinge of Alberta.

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THE CHAIRMAN: Has the Doctor had an opportunity of studying this program.

MR. FRAWLEY: Of studying the program..

THE CHAIRMAN: Yes, and the Commission.

MR. FRAWLEY: Yes.

Q (MR. FRAWLEY TO DR. BROWN): That is the whole program and that is the Commission and there you are?

A Which one are you referring to now.

Q I was reading from "K", you see the Commission is, if I might put it on the record, the Commission is the important thing. The program has been our attempt to put into a little more ordinary form the contents of the Commission, so that it does not really matter. I think you will find the program is as good a guide as any but the Commission is perhaps the better thing to look at, it is a little less hodgepodge perhaps but take on page 2, 3 (g):

"The Price and/or cost of petroleum products sold to
"jobbers and dealers in the said Province and the
"factors which enter into the determination of the
"said price and/or cost and what the fair and equit-
"able price and/or cost of petroleum products sold to
"jobbers and dealers in the said Province should be".

Now it is true that we have to analyse the question of refining but what the Commission, the Chairman has suggested to you perhaps is, that it is not enough to just make a good, careful analysis of refining practices, to determine that there is no undue waste, undue wastefulness, unnecessary expenditures in the refining, but after all it has to be related and carried on into the marketing price so that when we see 9.1 cent which is being charged to the jobbers,

"is that too much or too little." Now you say, well I have answered this to some extent by relating the refining cost, plus the costs of crude, the refining costs at least to the capital investment and that is a step forward, subject to what you are going to do with regard to the other plants but can you help us at all in the further problem of trying to ascertain what the jobbers should pay for a gallon of Ethyl Gasoline as compared to what he should pay for a gallon of Regular or Standard tank car or a barrel, and the same with the third structure, now can you put the two parts of the problem together for us without going unnecessarily out of your field; although I have a lot of confidence in you, Dr. Brown, I do not think you at any time will get very far out of things you know about?

A Well that is a long question.

Q Yes, it is just really a resumé?

A If I can perhaps tackle this, 3 (g) which you brought out.

Q Yes?

A And confine my remarks to that paragraph.

Q Yes?

THE CHAIRMAN: How does it read.

MR. FRAWLEY: 3 (g), it reads:

"The Price 'the controlling words you are familiar with, Mr. Chairman, but the actual words are:

"The Price and/ or cost of petroleum products sold to
"jobbers and dealers in the said Province and the
"factors which enter into the determination of the
"said price and/or cost and what the fair and equit-
"able price and/or cost of petroleum products sold to
"jobbers and dealers in the said Province should be."

THE CHAIRMAN: Yes.

MR. FRAWLEY: And going on to the program, that is dealt with under (b) represented by, well it is dealt with also there.

THE CHAIRMAN: The program does not matter.

Q MR. FRAWLEY: All right.

A The language used in 3 (g) would indicate to me that "price" and "cost" are used to indicate the same thing, in other words the 3 (g) has reference to the price paid by jobbers or the cost to jobbers. Now if that is the interpretation which is to be put on that language it would seem to me that it is a marketing problem almost wholly. If the interpretation is that the "cost" refers to the cost of production of the products, not the cost from the standpoint of the jobber but the cost from the standpoint of the refinery, I think I have already discussed that to some extent and it is my very definite opinion that if 3(g) is to be interpreted as meaning the cost of producing the various petroleum products, that all of the petroleum products produced from a barrel of crude must be considered at the same time, that it is utterly impossible to determine the cost of producing any one of the various products unless in the same statement and in the same sentence the cost of producing all of the other products is also considered and that the cost of producing the products will depend upon the products which are produced, the relative proportion, and the type of crude run and also the type of plant in which it is processed but all of the products must be considered at one time. It is utterly futile to attempt to set a cost of producing any one product out of the numerous products which are produced from

crude oil.

Q THE CHAIRMAN: Now you might take 1 (c), as my associate points out, we are simply directed to find:

"The cost of refining and processing crude petroleum "in the said Province and particularly the adequacy "and efficiency of present refineries and the reason-"ableness or otherwise of depreciation and other "charges included in existing refining costs, and "what the fair and equitable cost of refining and "processing crude petroleum in the said Province "should be."

A Now that can be done.

Q THE CHAIRMAN: Because you say that includes all of the products?

A That refers to petroleum which is the material which is processed but the gasoline is not a material which is processed, nor is any other one product.

Q Yes. Now then let us understand it, then you come over to this 3 (g) which we have been discussing:

"The Price and/or cost of petroleum products sold to "jobbers and dealers in the said Province and the "factors which enter into the determination of the "said price and/or cost and what the fair and equit-"able price and/or cost of petroleum products sold to "jobbers and dealers in the said Province should be."

Now that is what I am querying you about now, and what would you say are the factors which enter into the determination of the price. Now one of the factors, in most articles in the world, which enters into the determination of the price is the cost of the production of the

[illegible]

article?

A That is, to look at it from that standpoint----

Q That is basic.

A That is right and it also does----

Q It has some relation, your costs may be very much greater than your cost of production, but they will never be less?

A Not for long, that is trae and that condition does apply to the petroleum industry but that is the cost of producing all of the products.

Q Yes, I understand that, and you say----

A So long as you keep all of the products from petroleum together and consider them all at once, then these questions can be handled.

Q Yes, I understand Doctor, and you understand too that in order that you may help us, and I want you to understand, that it seems to us quite clear that His Honour the Lieutenant Governor of this Province wants us to make answer, and perhaps we cannot, we may never be able to, but he wants us to make answer as to what is the fair price of say gasoline and these various other things, that the different kinds of people in this Province use, the owner of a motor car is not concerned with the farmer's fuel, the farmer is not concerned in some instances at any rate with the gasoline that the tourist uses----

A And neither of them----

Q I have no manner of doubt that this Commission intends that we shall make answer to those questions and as I understand you, you cannot determine what the cost of any of them were if we are to make answer as to what the fair price is, we will have to arrive at it by different means and without re-

lation to the cost of that particular article?

A That is right.

Q Our nearest approach to cost is what it costs to make all of the products that emerge from a barrel of crude oil?

A That is right.

THE CHAIRMAN: Quite so.

Q MR. FRAWLEY: In other words if Mr. Halverson was also the refiner and the operation was a little smaller and Mr. Halverson not only sold the products but he refined them, I take it from you when he started out to sell he would leave the refinery and the refinery costs, and the refinery experience behind him and simply say "I have certain products to sell, now let me see what the market requires me to sell them at"?

A Except in the aggragate. The manufacturer of shoes puts eyelets in the shoe and he puts a shoe string in it and he adds the tops to the shoes and the heel and the soles, now when he goes out, what does he sell, he sells a shoe, which is the total production. He doesn't sell 5 cents for the pair of shoe laces in the shoe and 15 cents for the eyelets, he sells a pair of shoes but it so happens in the petroleum field you do not do that, you sell the eyelets separate from the shoe laces.

Q But that boot man knows what the eyelets cost?

A Not if he manufactures them himself.

Q Surely he would, surely he would know what his eyelets cost but you say "no" if he was manufacturing them as one operation at least?

A That is right. In order to determine the cost of his eyelets he would have to assess a certain overhead to that department, and he would have to do it in an arbitrary manner;

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in other words, he would have to assess the cost to the manufacturing of all the other parts of the shoe and then by the difference load the eyelets for the balance, and usually in manufacturing processes, the price is the exact price of the operation, but in refining crude oil,- usually the manufacturer goes out and buys something, then buys something else, and weaves them together into a finished product like a motor car, but in the petroleum industry, it is the exact opposite, he goes out and he buys one product, the crude oil, and breaks it down into a number of products to serve the community, and the whole thing is the reverse of the ordinary manufacturing operation, and as a result the ideas that would apply to the manufacture of moter cars has to be put into reverse, and you cannot consider the problems from the same points of view.

Q The packing industry is very similar, is it not,

A Yes, where they buy a carcass and break it down to the component parts. Now, what is the cost of producing a rib roast as compared with sirloin steak or round steak, what determines, why is a rib roast more than a round steak, and it is the same principle exactly.

Q So I have been told.

Q THE CHAIRMAN: All right, then, the reason for paying more for the rib roast than the round steak, I suppose, is that there is a greater demand for that?

A Yes, economic factors.

Q Yes, a greater demand, and what other people sell rib roasts for?

A It is talking of the supply in relation to the demand.

Q Yes?

Q MAJOR LIPSETT: These instances, of course, Dr. Brown, are all based on genuine and complete competition?

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A Well, there may, or may not be, competition, in the packing industry or the petroleum industry. I do not think that competition is excluded from any one industry and confined to others, that is, there may or may not be competition, and I think that is a separate factor, and that again is determined very largely from the marketing end of it because competition is really felt only in the market.

Q THE CHAIRMAN: Well I was recently reading an article to Mr. Frawley in which a very great man said that competition was now dead, true competition, however, that is not your field.

MR. FRAWLEY: I will ask Dr. Fry about that.

Q (MR. FRAWLEY to Dr. Brown) I want to ask you something which may overlap with marketing, but I think in view of the very last question, asked you, that people pay more for this petroleum product than for that petroleum product, it is largely a matter of taste, and so on, will you let us have your views on the need in the Alberta market for high octane gasoline?

A Well, perhaps I had better begin that answer from an explanation of what the difference between high octane and low octane gasoline is, and what effect it may have on the operation of a car.

Q You see, we do know that high octane, you can almost take that as evidence from me, that high octane gasline, Ethyl gasoline, sells for more in this territory than standard gasoline, and standard gasoline sells again for more than third structure, and following up this question of the utility of endeavoring to ascertain

the cost of these three products separately, I think it would be of some value to the Commission to have the benefit of your views as a chemical engineer, of this business of having, of selling high octane gasoline, which in this territory is called "Ethyl gasoline" and the need for it, the need for people paying that much more, if there be any, or if it is a pure question of caprice, and so on, let us hear what it is all about?

A Well, I can begin, perhaps, by explaining, if I can, the difference between high octane and low octane gasoline and the motor performance, which is the only evidence that a user has that he is using the high or low octane gasoline, perhaps I may be of some help. It is a question which may be answered in a number of different ways, perhaps by individuals who hold different opinions, and before I would answer the question, I would like to set forth the basis for my opinion.

Q Yes?

A To begin at the beginning, a motor car operates on what is known as the Otto-cycle, it is usually the Otto 4-stroke cycle. It is called a cycle because the engine keeps repeating the same series of operations over and over again in a cyclitic manner. It is called the 4-stroke cycle because there are 4 strokes to the piston to complete one cycle, and it is called the Otto-cycle after the man who was originally successful in building an engine to operate in this manner, a German.

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Now, in this...........

Q Oh, it is not a-u-t-o?

A No, it is o-t-t-o - cycle. In this cycle, if I might use my hands as part of the engine, I think I can make it clear. The top of the combustion chamber or the head of the motor, which will be represented by my left hand, held so, and the piston will move up and down underneath the head of the combustion chamber or the cylinder head, as it is called. We start with the piston near the top, at the top dead centre, a vacuum in the combustion chamber above the piston and below the cylinder head as a clearance vacuum, and at that point the intake valve is opened and as the piston moves down on the first stroke of the cycle, it sucks air through the carburetor, it takes up the liquid gasoline and vapors, some of them, and carries the rest as a fog or mist in the air until this mixture is drawn into the combustion chamber by the downward movement of the piston on the first or intake stroke We now have the combustion chamber full more or less with this explosive mixture, and during this intake stroke, where the piston moves down, the pressure of the atmosphere does work on the piston, and pushes the piston down. Now we have to compress this mixture and during the compression stroke, both valves, the intake and exhaust, are closed, and the piston is forced up against the explosive mixture in the combustion chamber, taking energy out of the fly wheel and compressing this explosive mixture to a high pressure. During this stroke, the piston does work on the mixture which is proportionate to the pressure of the mixture in the

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cumbustion chamber and to the decrease in volume of the explosive mixture brought about by the upward movement of the piston. At this point, both the valves are closed and the explosive mixture is at a high pressure of about, let us say, 100 to 120, andthen the ignition spark is passed into the pressure part of the chamber, and this mixture explodes or burns, and during that explosion or combustion, the temperature is increased, and due to the increased temperature, the pressure is greatly increased. Then this high pressure of the gases pushes the piston down on the third stroke or power stroke and because the pressure on the piston during the power stroke is greater than the pressure on the piston during the compression stroke, more work is done on the piston as it is forced down during the power stroke than was done on the explosion mixture by the piston during the compression stroke, and at the end of the power stroke the piston is at the bottom dead centre, and the exhaust valve is open, and then the piston moves back, pushing the burned gases out of the cylinder against atmospheric pressure and in the ideal cycle the work done on the piston by the atmosphere during the intake stroke, the first stroke, is equal to the pressure done by the piston on the gases during the exhaust stroke, so that those two factors cancel out, and the work done by the engine is equal to the difference between the work done by the piston, by the gases on the piston during the power stroke when the piston is forced down.

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And the work done by the piston on the expansive mixture during the compression stroke - well these work terms are proportional - would increase or decrease in volume of the mixture. So that if we take the power stroke that allows the piston to go down a greater distance we are going to get more work out of the expansive mixture than if we take the piston down a shorter distance. The same thing is true of the compression stroke, in the reverse direction. If we compress the mixture more we do more work on the mixture than if we compressed the mixture to a lesser degree. However, the work done during the power stroke is always greater than the work done by the piston and gases during the compression stroke because the pressure throughout the power stroke is greater than the pressure during the compression stroke. So that if we build an engine then with a large increase and decrease in volume as the piston moves up and down we are going to get more work out of the same amount of expansive mixture. We are going to have a more efficient engine and an engine that will do more work and have more power. So that it would be very simple, a nice easy simple proposition to simply build motors of what we call high compression ratios or high expansion ratios, which means that the volume of the combustion chanber when the piston is at bottom dead centre is large compared to the volume above the piston of the combustion chamber when the piston is at top dead centre and the compression ratio represents that large volume to the small volume between the piston

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at bottom dead centre and top dead centre. Now a compression ratio of 6 or 7 or 8 is regarded as a fairly high compression ratio for automobile engines. The higher the compression ratio the more efficient will be the use of the fuel and the greater will be the power output of the engine. Now with the motor car manufacturers desiring to put on the market cars which have high power output with a relatively small engine would want to use a high compression ratio that will give them more power. Furthermore it will also give them a more efficient engine with the result that the miles per gallon will be greater and that is the only means we have of increasing both the power and the efficiency. If you put in a larger engine we will get more power but you will not get more miles per gallon. In fact you are apt to get less because you have heavier engines to carry around. So that the industry as a whole has been focused on this matter of high compression ratio. There is one limitation or difficulty to the use of high compression ratios aside from any mechanical limitation and that is the burning characteristics of the fuel. If we have this mixture compressed to a high degree and ignite the mixture at one point by means of a spark, we find the flame will spread in all directions away from the spark on an expanding surface and as this mixture burns from the spark plug it becomes heated and expands and compresses the unburned mixture that has not yet been ignited and this unburned mixture is compressed to higher and higher pressure and also becomes heated to a higher temper-

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ature while the first part of the mixture burns. Therefore, this compression due to high temperature under pressure closes the association between the oxygen molecules and the molecules shift and we find the fuel actually becomes partially oxidized and forms a combustible compound much in the nature of a high explosive. So that after this combustion has proceeded to a certain extent under these high temperatures and pressure conditions, the unburned mixture simply detonates or lets go with a bang in the same manner as a high explosive. So that really we then have part of the mixture at a moderate pressure of about 500 pounds, that part that burned first in the normal manner, and the last part of the mixture which detonates perhaps at a pressure of 2000 pounds. If we have a pressure difference of that nature in any gas volume the high pressure gas will immediately expand in the same way as the high powered gas leaving the muzzle of a large caliber rifle forces back the low pressure gas. And we get a sound in these combustion chambers set up by the same means as the sound of a large caliber rifle when it is fired. There is also accompanying this detonation a resulting expansion loss in power because the high pressure of the last part of the mixture burned, which is 2000 pounds, is dissipated by compressing that part of the gas which is only 500 pounds pressure and just as the work done during the power stroke is greater than the work done during the compression stroke, we find that the work done or the work energy expended by the high pressure gas due to

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the detonation on the low pressure gas is much greater than the resulting work done on the low pressure gas with the result that there is actually less energy available to do the work on the piston following this detonation than there was when the combustion was normal. That energy which is apparently lost or dissipated in the sound wave and the high velocity pressure wave which is set up, has the same effect on the combustion chamber as though the surfaces of the combustion chamber were being hammered by a heavy hammer. It heats the surfaces of the combustion chamber and dissipates energy in that manner. That is one of the important limitations to the use of high compression ratio engines. In order to overcome that we have either to use fuels which do not form the unstable oxygenated compounds frequently referred to as peroxides and detonate or else use some kind of addition material which will inhibit or retard this action. Lead tetraethyl used in Ethyl gasoline is an addition compound which tends to prevent detonation, and the use of the cracking process which makes a chemical change in the composition of the crude oil and its materials, produces a gasoline of such a chemical structure that it has less tendency to detonate than straight run gasoline. The use of other materials such as Benzol has the same effect. Now the value of this gasoline to the user is dependent solely upon the user having a car or an engine of such high compression ratio that the ordinary fuel will not knock or detonate. Otherwise there is, of course, no benefit of him using a fuel of these special characteristics if the fuel of

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ordinary characteristics fully meets his requirements. Therefore, the widespread use of these high compression ratio motors had to wait upon the wide, distribution of fuels of a rather high octane number. With the universal distribution of fuels of about 72 or 73 octane number, as represented by the regular grade, we now find practically all motor cars equipped with motors of such a compression ratio that they can utilize to the maximum efficiency regular structure gasoline. And in some cases if a man has a higher compression ratio motor or adjusts his car so that it has a greater tendency to knock or detonate, he will find that he should use perhaps the Ethyl gasoline or some specially high octane gasoline in order to get knock free service from his car. On the other hand, some people may so adjust their cars or use cars with a low pressure ratio or put in two or three cylinder head gaskets underneath the cylinder head so that they could operate in a satisfactory manner without knocking on third structure gasoline. But the man who has reduced the compression ratio of his motor or is using an old car with a low compression ratio is not getting the efficiency out of his power that the man is who has a modern motor with a higher compression ratio. There are, however, a great many other factors which will determine the efficiency, carburetor adjustment and the general condition of the engine. In the laboratory in making careful tests, it appears that the actual net improvement to the ordinary motorist does not exceed about 10% when the octane number is increased from about

55 up to about 70.

Q MR. FRAWLEY: The net improvement to the ordinary motorist is ---

A In general the performance of power output is about 10% when everything is adjusted to take full advantage of the increase in octane number from about 55 to about 70. Along with which there is also a corresponding increase in efficiency or decrease in fuel consumption so that the over-all benefit is perhaps in the neighborhood of about 15 or 16% on the particular type of car that I was using in these tests, but I believe it is generally representative. Similarly as the octane number is increased above 70 there is roughly a corresponding improvement in performance. Now there are other factors than the improvement in performance of the car which must be considered in determining the value of any particular product to a user. If every user was an engineer and did not care about style and his wife never drove the car and all he was concerned with was power and mileage, perhaps that figure of 16% for the octane number difference between 55 and 70, or 55 and 72 would be the whole story. But the increased power of 10% during the accelerating period when you are starting up from the red stop light at the corner will make all the difference in getting ahead of the procession or being crowded off the edge of the road and taking third or fourth place. So that a great many individuals are willing to pay perhaps 25% more for the increase in power and efficiency which may amount to only 10 or 15%. So that the actual value

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between these different fuels of different octane number, that is the actual value to the consumer is going to be determined in the long run by the consumers themselves and what they are willing to pay for these rather small differences in the individual cases between these fuels. It is my opinion, which is well considered after a good deal of work in this field, that there is no necessity for any high octane gasoline over and above the regular grade. In other words, I believe that all cars could be operated in a reasonably satisfactory manner with regular grade gasoline. However, by special adjustments and due to the individual differences in various cars and the preferences of many different drivers there is a certain group of consumers who are willing to pay more for fuels of a higher octane number because in their particular cars and the way they drive they think they get better performance. The rational answer to the question is, of course, all automobiles requiring the same octane number of motor fuel, a uniform octane number which has been made possible by the use of lead Tetraethyl in bringing up to a certain standard all commercial gasolines of regular grade. Then, of course, on the other side of it there is the man who does not care so much about style and the little extra performance he gets perhaps from using even regular grade gasoline. He may retard his spark and put a couple of extra gaskets under the cylinder head even on a modern motor and use third structure gasoline. Now it all depends on how much trouble these other people are willing to go to, although they could use third

[illegible]

structure gasoline and the difference in price between third structure gasoline and the standard grade as to how much third structure will be sold. I believe that perfectly satisfactory performance could be obtained on all present vehicles if properly adjusted by the use of regular grade gasoline. Therefore, I consider that there is no necessity for high octane gasoline provided there is available a gasoline of about 72, 73 or 74 octane as a regular grade. Therefore, for those people who wish to use a high octane gasoline there is no reason at all why they should not be supplied with it.

Q MR. FRAWLEY: Is there any additional value in the fact that we are in a high altitude in this province?

A At high altitudes the pressure is less and therefore, the tendency to detonate is less. I believe as a rough indication this is about 4000 feet.

MR. NOLAN: 3400 feet.

A Let us take a round figure, 3500. I should imagine that would mean driving on the level under comparable conditions at an octane number about 7 less here than at sea level would give corresponding performance. So that if 75 is required to give comparable performance at sea level perhaps somewhere around 68 would be adequate here. On the other hand, this country has a good many hills and mountains and whenever you are in a mountainous territory, the requirements on the engine are much heavier and you usually require a higher octane number to get equally satisfactory performance. I know a

number of people in the East who drive through the Alleghany Mountains and will use regular structure when they are driving on the level but when they are making a trip through the mountains they will tank up with Ethyl because of the superior performance obtained in the mountains. The fact of there being mountains here may to a certain extent neutralize the advantage of the high altitude.

(At this stage the hearing was adjourned until 2:00 P.m.)

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(EXAMINATION OF DR. BROWN CONTINUED BY MR. FRAWLEY)

Q MR. FRAWLEY: At the noon adjournment I was just about to call your attention to the octane number in the specifications, Exhibit "302" which is a statement of specifications of the Imperial's products and you see there that the octane number is from 76.5 to 77, both summer and winter, there does not appear to be any distinction, and the 3-Star Gasoline 71 to 71.5, well now looking at their Esso Gasoline, which they call Esso, where it runs in octane from 76½ to 77, and if you will assume with me that one marketer in this Province, if you will assume with me that one marketer in Alberta, his Ethyl Gasoline is 83 octane number as compared to the 76½ or 77, now what are your views, following up what you have said this morning, as to the values to be obtained from increased octane number, what do you say as to the, oh, the practicability, value of that increase in octane numbers between those two Ethyl gasolines, each selling in the market at the same price of course.

THE CHAIRMAN: Which two?

MR. FRAWLEY: The 76.

THE CHAIRMAN: Exhibit "302".

Q MR. FRAWLEY: On Exhibit "302" and he will have to assume with me, I put it to the witness to assume with me that the Texas Company sells its Ethyl Gasoline with an octane number of 83?

A Well I am assuming that these octane numbers are determined by the same method.

Q Yes?

A And also secondly that they properly represent the road

octane number, that is the octane number as reported is a determination made in the laboratory and it is known that the equivalent octane number as determined under actual operating conditions on the road will be different for different cars and in the average may even be different than these values determined in the laboratory.

Q Yes?

A Making the assumption with you that the octane numbers are properly representive of the road conditions and that they are determined by the same method, the 83 octane number as compared to the 77, which shows an octane number difference of about 6, would indicate, would be of such a degree of difference that it could be determined by drivers who were operating their cars at a point where one of those fuels would knock and the other would not. Expressed in percentages it is almost nothing but an intelligent guess but it would be about perhaps 3 to 4 per cent difference in performance, which is just perhaps beyond the experimental error in making comparative tests. The value of one as compared with the other would depend again entirely upon the conditions of use, the psychology of the purchaser, car adjustment and so on but there would not be very much difference in the two fuels.

Q No, well now, you put it to us this morning that in your opinion, looking at the picture overall, that there was no need for a higher octane gasoline than regular grade of 72 octane number and starting from that, what do you think as to the necessity for an 83 octane gasoline in the Ethyl grade, Ethyl Gasoline grade, or what we call first structure?

A Well my same statement would apply to that, certainly if

there is no need, and by "need" I mean necessity of such a product for the reasonable satisfactory operation of automotive equipment, if there is no need for a 78 octane as compared to a 72, there certainly would be no need for an 83 as compared to a 78.

Q Yes. As you go up in octane numbers, it may be that next year a marketer would come on with a 90 octane gasoline, that could be made commerically I suppose?

A Oh yes.

Q What does aviation gasoline run in your experience?

A Well it varies from 87, 100, 125. I believe the standard is 87 for most of it now, is it not.

MR. McGRATH: We sell more 80 than 87.

WITNESS: Yes, there is an 80 product too, unleaded Ethyl 74 octane. I know there is 87 and then there is one around 93 or so and 100 and I believe they have done some experimental work with 125.

Q Yes, now that is aviation gasoline but I mean in view of the way that these octane numbers are jumping, it might be that a marketer will come on next year with an octane gasoline, with a gasoline of an octane number of say 90 and again not wanting to explore our marketing discussion, but wanting the benefit of your views as an expert, chemical engineer, what would you say as to this, what would appear to be an octane race among these refiners and marketers?

A Well from an engineering point of view it seems to me that practically all motor cars are designed to operate satisfactorily on what is known as regular grade motor fuels, which now has an octane number usually, I think it is 72-74 by (free) L-3 method, so that it would seem from a chemical stand-

point that if the cars are designed to operate satisfactorily on a fuel of such octane requirements and that all such regular grade fuel has that octane requirement, that there would be no need for an appreciable supply of fuel of higher octane rating and in this territory where we have an altitude of 3500 feet approximately, that statement should apply with even more force than at the sea-level.

Q And you are aware of course that in this territory the differential between Ethyl and Regular is 2½ cents?

A That is what I understand, yes.

Q All right.

Q THE CHAIRMAN: Have you heard any suggestion, Dr. Brown, that manufacturers of cars are interested in Ethyl and so they construct their cars only so that that product can be used?

A I have heard assertions of that kind and I believe there are a number of individuals who really believe that. It is my own opinion, and I am really close to some of these manufacturers who have an interest in the Ethyl fluid development, that their attitude is to put out a car which will operate satisfactorily on Standard, Regular grade fuel but in some cases to build that car so that it can also take advantage of high octane fuels when, as and if they are available and if the car user wishes to use them; in other words their cars are designed so that they can operate entirely satisfactorily on regular grade fuel but that they can also, by proper adjustment, get superior performance to a degree from fuels of higher octane numbers so that again my statement that there is no need for the higher octane fuel I think still applies but I do not mean to imply that some users may not really get a benefit from the high octane

fuel of one kind or another and may be entirely justified to pay the higher price for it because of their particular conditions but I also believe that these same users can get by in a reasonably satisfactory manner with their equipment by changing the adjustment on the regular grade fuel.

Q MR. FRAWLEY: Let me ask you this, Dr. Brown, if a 72 octane gasoline costs x cents and we know the difficulty now, but if it could be determined, to have cost X cents per gallon, what would 83 octane cost?

A Cost?

Q Yes, cost?

A Why anything from X minus something to X plus something, I do not know what it would cost, you mean by cost----

Q I am assuming, now it may not be at all, but can the difference in octane number------

A Be evaluated?

Q No, can it be brought higher by the addition of leaded tetra-Ethyl ?

A Yes, in some cases.

Q In those cases where it might be----

A It would go from 72 to 80.

Q From standard to 83?

A Well that only in certain cases and----

Q I mean cost in the refinery you know?

A Well wait a minute, if I understand your question, this is a hypothetical case which may exist and again may not.

Q Yes?

A And it means we have a particular gasoline of 72 octane.

Q Yes?

[illegible]

A Which can be increased to 80 by simply adding lead to it.

Q Well let us see if that cost----

A That is an assumption and it may exist and it may not, and then you want to know how much lead would have to be added to bring it from 72 to 80.

Q Correct?

A That might vary from some very large quantity which it would be impractical, down to perhaps a minimum I would imagine of about $1\frac{1}{4}$ to $1\frac{1}{2}$ c.c. to a gallon, that is a wine gallon, that would be about $1\frac{1}{2}$ to 2, would it not, that would vary, yes, from about $1\frac{1}{2}$ to 2 c.c. at a minimum per imperial gallons. I cannot think offhand now whether such a fuel can be obtained but there might be such a fuel produced.

Q MR. NOLAN: May I ask the Doctor, if that assumes that there was no lead in the 72 octane gas in the first instance?

A Yes, that would assume no lead in the 72 octane and a fairly good susceptibility at that.

Q MR. FRAWLEY: Assuming, what is in my mind, assuming, it is difficult you say but what I would like to get is some idea of the refining, of the values in the refininery, at the refinery door, the refinery exit door, of those two gasolines?

A Well I tried to make clear this morning, Mr. Frawley, that I think it is utterly impossible to differentiate that way unless you fix everything else. Now in order to produce an 80 octane gasoline I know that in actual practice it is necessary to either select special crude or put it through a special process and then add some lead to it. Now what is the cost of the special crude and the special process all

depends upon what the cost for the other products are, and we are in that same predicament, to answer that question as we were as to what is the cost of producing gasoline versus kerosene or furnace distillate.

Q You cannot just say that the 83 octane gasoline has more value or did cost any more to make, in the refinery, that is to make it, than the 76 octane gas, to the manufacturer who is making it?

A No. It all depends upon conditions.

Q Yes?

A It is conceivable that one manufacturer might produce a gasoline at 80 octane at less cost than another manufacturer may produce one at 76.

Q Would you say that this octane rate is going to lead necessarily to a rapid obsolescence of refining plants and early reconstruction, earlier than ordinarily, reconstruction of plants?

A Yes, it has done that.

Q And we might expect it will do that in this territory?

A I think it is doing it.

Q It is doing it in this territory?

A Yes.

MR. FRAWLEY: Well that is very interesting.

MAJOR LIPSETT: Mr. Frawley, I do not think your question was quite what Dr. Brown answered. He said that one manufacturer might make 80 or 83 octane gasoline cheaper than another manufacturer might make 76, but I think what you were putting to him, was it not, in the case of one manufacturer making both.

MR. FRAWLEY: Yes.

MAJOR LIPSETT: Both octanes,a high octane would cost more than the other.

MR. FRAWLEY: Yes, I was interested, clearly he has, Dr. Brown has answered the question but he has given a 72 octane gasoline unleaded and we desire to make it into an 83 octane gasoline by the addition of leaded tetra Ethyl.

A It is the additional cost of the leaded tetra to be added and I figured a minimum of 1½ to 2 c.c. per imperial gallon .

Q To complete it, what is the laid down cost of leaded tetra Ethyl per c.c. in this Territory?

MR. McGRATH: 28 point.

WITNESS: 28-100ths of a cent per c.c.

MR. McGRATH: Yes.

Q MAJOR LIPSETT: Can you bring that now into the increase of the cost?

A Well if it took two c.c.'s of Ethyl fluid per imperial gallons that would mean an increased expenditure for lead of 66-100ths of a cent.

Q Half a cent?

A A little over half a cent, and there would be some handling charges and so on in blending that, which would increase that somewhat so that it is conceivable that it might be possible if a refiner had a particular fuel of about 72 octane and the proper lead susceptibility, that he might be able to convert 72 octane into 80 at a cost of 3/4 of a cent a gallon or thereabouts.

MR. FRAWLEY: Now are you sufficiently familiar with the Imperial operation to know how they make

their 3-Star Gasoline, whether it is by simply taking straight run and adding lead tetra Ethyl or whether it is a blend of straight run and cracked, to which lead is added or what?

A Well I think one of their men can answer that question more assuredly than I can but I have seen their plant and my recollection is that their regular gasoline is a blend of straight run and cracked with the addition of the proper amount of absorption, of stablized absorption and lead to bring it up to their requirements.

Q Yes, that is about right, is it not?

MR. McGRATH: That is right.

THE CHAIRMAN: That last answer I didn't get.

MR. FRAWLEY: The last answer.

A That the regular grade----

Q 3-Star Gasoline?

A 3-Star Gasoline is manufactured by the Imperial refinery at Calgary by blending their cracked gasline with straight run gasoline and also blending the proper amount of stabilized absorption naphtha and the required amount of lead tetra Ethyl to bring that to the desired specifications. I might add that I believe in this particular case at Calgary it is impossible from any commercial standpoint to convert that gasoline into 80 octane by simply adding lead.

Q You think you cannot convert that gasoline, that 3-Star minus its lead, increase that to 83 octane by adding lead?

A Well that is the same thing, I believe that it is commercially impossible to convert 3-Star gasoline of 72 octane or thereabouts, 71 to 71½ as given here, to 80 octane by simply adding lead to it, or as you said, taking the lead out and

[illegible]

then putting it back in and then putting some more in.

Q It is the same thing, so perhaps it is not an unfair assumption that the Imperial had this octane rate to contend with, or had it in mind, when they decided to build the new plant, the more modern plant in Calgary?

A I believe that is one of the important factors.

MR. McGRATH: With the improved tractors, tractor gasoline requires better octane gasoline.

WITNESS: Yes.

MR. FRAWLEY: That is still an octane rate.

MR. McGRATH: Yes, the lower grade gasolines have to be a better quality, the third structure gasoline has to be a better quality to meet with the improved tractor designs.

MR. FRAWLEY: Now if there is anything further on this question of high octane versus low that anyone wishes to ask about I wish they would do so now because I now intend to proceed with Dr. Brown to another matter, an entirely different matter, and that is the price of crude, the field price of crude.

MR. MACLEOD: May I ask Dr. Brown a question or two, I mean growing out of the examination this morning.

THE CHAIRMAN: You are appearing, Mr. MACLEOD

MR. MACLEOD: For the Texas Company of Canada.

(MR. J.E.A. MACLEOD, K.C. APPEARS FOR THE TEXAS COMPANY OF CANADA

Q MR. MACLEOD: Dr. Brown, I gather from your account of the refining process given this morning that, assuming two refineries were putting through a fairly equal volume and with equal efficiency, that the cost would vary according to the quality of the crude?

A You mean the cost of manufacturing?

Q Yes?

A The processing cost.

Q Yes?

A The processing cost will vary with the character of the crude.

Q And the crude varies in character according to the different fields?

A That is right.

Q Turner Valley I think you told us is of a different character from some other fields?

A That is right.

Q And that would be reflected in costs?

A In the processing costs, yes.

Q Now with regard to this octane question, I was not here unfortunately when you were asked the first question but I understand that the Sky Chief of the Texas Company was mentioned, was it.

A I do not recall that particular name being mentioned.

MR. FRAWLEY: Not by name.

THE CHAIRMAN: The Texas Company was mentioned.

A The Texas Company was mentioned.

Q MR. MACLEOD: Now anything you have had to say about that, I presume is based entirely upon the octane number, I mean you are not talking generally about any product that the Texas Company may sell?

A No, my answer to that question was limited to the assumptions given me in the question and which I believe I stated in my answers.

Q That one had an octane number of such an amount and the other

something else?

A That is right.

Q Now I would also like to be clear on another matter, the octane number is not fixed entirely, is it, by the addition of Ethyl fluids?

A No, that is one means of improving the octane number.

Q And two gasolines might have a similar octane number and in getting that octane number in one, they might have to use more of the Ethyl fluid than the other?

A That is right.

(Go to number 9167)

Q So that it is quite possible for a manufacturer by the result of research and so on and modern equipment, to produce a higher octane gasoline than another, octane number gasoline, without reference to the amount of ethyl fluid introduced?

A That is right. High octane number gasoline may be produced without any ethyl fluid.

Q You talk about there being no need of anything more than the standard grade. I presume you would have said that ten years ago wouldn't you? It is only a relative matter is it not?

A Ten years ago. Let me see. I do not believe there really was a standard, universally recognized octane number ten years ago.

Q I mean I am not talking so much about octane number now but the quality of gas we had then served our then purpose?

A Yes.

Q And there was no need of anything better?

A At that time that is right.

Q So that if some method had been employed to stabilize the quality of gasoline at that time, we would still be there, wouldn't we, and never have any improvements?

A If there was no change there would be no change, certainly. I think what you mean there, if any action had been taken to prevent the marketing of different gasolines then there would have been no improvement.

Q What I really mean is this, when you speak of need, you simply mean we can get along today with that particular gasoline?

A Yes, our needs change from time to time.

Q And when our needs change it is only by the product being improved that our needs do change?

A Yes. The needs of tomorrow are the luxuries of today, perhaps.

Q MR. FRAWLEY: Now, Dr. Brown, one of the other things which the Commission is concerned with, is analysing......

THE CHAIRMAN: Perhaps Mr. Nolan wants to ask some questions?

MR. NOLAN: No, I do not think there is anything on that, thanks.

Q MR. FRAWLEY: Now, the question of the posted field price of crude. Now, we have already spent quite some time analysing the present posted field price of crude which is $1.20 for 45 gravity, and $1.30 for 48 gravity. But we will stick to the $1.30?

A 48 gravity, $1.30.

Q Well, we have been talking all the time about 48 gravity, because Mr. McGrath's computations were based on 48. I do not suppose it matters a bit which one you take so long as you stick to it all the way through.

A Well, we will stick to 48 gravity, Turner Valley crude as representative of what we are talking about.

Q Yes, that is what we are shooting at and analysing. Mr. McGrath came and first explained to us how the price was posted and why, in January 1938. In January 1938, the Imperial posted this price of $1.30 for 48 gravity crude, which had been up to that date

$1.52. And then Mr. McGrath told us, and I think you heard something of this yourself when you gave evidence before the Tariff Board in Ottawa, that was with a view to expanding the market for Turner Valley crude as far as it was then thought reasonable to go, and that the price came down, being the average of four prices. This is now purely historical. They averaged the value of $1.02 to serve what was called the Manitoba market with products refined at the Regina Refinery, and the price of $1.15 to serve the normal Regina territory from the Regina Refinery, and a price of $.92 to serve the Coutts area in Alberta from the Calgary Refinery, and $1.62 to serve the normal Calgary refining territory, and the average of those prices was $1.30 which was posted on the 5th of January 1938. As I say Mr. McGrath was asked to state the factors which entered into the posting of the present price, and he gave us that as the history of it. He also said he and his company had come to the conclusion that the average basis was not a sound way of posting price, and that they were not doing it, or not attempting perhaps I should say, to justify it on that basis. In fact he told us Turner Valley crude had now definitely lost the Manitoba market, and the simple fact is that the Manitoba market reaching as far west as Portage la Prairie in Manitoba, is now served from the Sarnia Refinery with Illinois crude. So following on that Mr. McGrath was asked to prepare some computations based on what, in his Company's opinion, was the competitive price in Manitoba and also at our request

built up a calculation based on $1.10, being the competitive well price in Montana. He did that, and you have in front of you Exhibit "268", which is a build-up of Turner Valley values starting with $1.00 crude at the well, and there is another exhibit which I would like to get for you, which shows the build-up for $1.10 at the well.

MR. NOLAN: I think it should be made clear that the two exhibits "268" and "269" were requested from us by Commission Counsel.

MR. FRAWLEY: Both of them, Mr. Nolan?

MR. NOLAN: Yes.

MR. FRAWLEY: I did not request anything on the basis of $1.00 because there was a friendly controversy between us as to whether the price was $1.00 or $1.10. Commission Counsel and Mr.Cottle never at any time had any information other than the effective well price was $1.10.

MR. NOLAN: Our point is that the $1.00 figure we gave was the corporate opinion of the Company, and was at the 5th of January 1938.

Q MR. FRAWLEY: Mr. McGrath told us when he filed Exhibit "268" and Exhibit "269" that the $1.00 that there was so much talk about, was the corporate opinion of his Company at the 5th of January.

THE CHAIRMAN: 19?

Q MR. FRAWLEY: And he saw no change to vary from that to now. He also said in the endeavour to review this that the $1.00.....

THE CHAIRMAN: On the 5th of January,

1938?

MR. FRAWLEY: The 5th of January, 1938. He also said one could only tell what that Montana price was by going out and buying some. With all that by way of background, I would like your views as to what you think the value - what this Commission should take to be the fair and reasonable - well just a second, what this Commission should find to be and recommend to be the fair and equitable field price which should be paid, taking the words right from the programme. There are doubtless various considerations involved there, and various ways of approach, and I would like you to discuss the whole matter fully?

A Well, the determination of a fair or reasonable price for crude in a field, is again every complicated question, because that price can be set on the basis of any one or any number of many divergent and even conflicting objectives. By and large, throughout the United States, they have reached the conclusion that the posted price for crude oil in the various fields should be sufficiently high so that sufficient capital will venture into the drilling operations so as to continually develop and find more crude reserves at a rate to maintain the reserves in sight sufficient for approximately 15 years, and that the price should not be so high as to encourage drilling beyond that rate. Well, of course, that is a factor which can operate only over a long range and over a wide territory in which there are a number of different fields. Every once in a while a new field is opened

up with crude at a certain price, and we have our various oil floods, the Seminole and East Texas and other fields. But that seems to be long range objective that is recognized by the Government Boards and the industry generally in the United States. And that same principle, I think, should be considered as one of the factors in the proper and fair price in Turner Valley. If the price is too low no new drilling will be carried out and only those producers who now have their wells in will produce oil, and the field will not be developed. On the other hand, if the price is too high, the field may be developed too rapidly and may encourage too much drilling and that will also be unfortunate. That is one of the factors which should be considered. It, perhaps, cannot be considered as the sole factor by any means, but it is one that should be taken into account. There is another very important factor, and I believe the one which can be handled in a more satisfactory manner, and I would suggest it as perhaps being the simplest, safest and perhaps the most generally satisfactory basis for estimating or setting a fair value for Turner Valley crude. And that is that every crude supply on the Continent is more or less bucking every other supply. The supply of crude down in Illinois is seeking a market and it has now displaced to a very considerable extent Mid-Continent crude from Sarnia, and as it goes into Sarnia at its price, which is lower than the Mid-Continent effective price, the products from that Illinois crude will back up through the

Great Lakes and come into Winnipeg, Manitoba. So that through that means, Turner Valley crude is bucking against Illinois crude. Similarly, there is a crude in Montana which can be refined at Regina and also the products from the Montana crude may be shipped into Alberta and through these means as well as other means, Turner Valley crude is really seeking markets and bucking against the Montana crude, such as Cutbank. So that a fair and reasonable price for crude oil in the field can perhaps be determined in the most satisfactory way by a consideration of the competitive conditions in or at various points. Comparing competitive conditions of products from Turner Valley crude and Turner Valley crude itself, with the products from other crudes and the other crudes themselves, I recommend that procedure because I believe that it is something tangible and if it is considered rather carefully will automatically include the other factors which I have mentioned. However, if it is decided that Turner Valley crude is to seek a much wider market than it is now supplying, that is to say Turner Valley crude is to be delivered on the Great Lakes and perhaps carried down to Sarnia in direct competition with Illinois crude at Sarnia, then we can arrive at the fair price on that basis by this same means I am recommending. That is the competitive conditions of Turner Valley crude with other crudes at certain locations. If it is decided Turner Valley crude is to reach Tidewater at Vancouver, to compete with California crude there, the same method can be

applied to that situation. Therefore, I recommend this as perhaps the most satisfactory way. And as an example of that, Exhibit "268" and Exhibit "269" show how a specific case may be considered. Referring to Exhibit "269" in particular, the competitive condition or the competitive position rather of Cutbank crude of 37 gravity at Regina as refined by the Imperial Oil Company at Regina has been calculated in relation to Turner Valley crude at Regina, and refined by the Imperial Oil Company at Regina. With the result that the fair and equitable price for Turner Valley crude on the basis as set forth in Exhibit "269" can be set in relationship to Cutbank crude. The same procedure can be followed out for any other territory or point where Turner Valley crude should be considered to supply the market. In my opinion, the well price of 37 gravity Cutbank crude of $1.10 is at the present time a reasonably low price. I doubt if any appreciable quantity of Cutbank crude could be purchased at a price less than $1.10. I mean by that, enough to supply a refiner running some 2000 barrels a day or possibly more. As has been stated of course, that price can actually be determined perhaps, only by someone going in and trying to buy crude. I believe that price under present conditions is about as low as could be expected to obtain such quantities of Cutbank crude, although I know there is crude being sold in that field locally for less than $1.00 a barrel. Now, to the price at the well has been added gathering and loading expense, freight to Regina and it shows that at Regina one barrel of Cutbank

crude would cost $1.92 laid down. Now this Cutbank crude can be refined in a number of different ways. It may be refined according to the process of the Imperial Oil Company at Regina, in which case it will produce certain products. It may be refined in a skimming or topping operation in which case it will produce different products, and therefore, the relative value between Turner Valley crude and Cutbank crude will be different for the different refineries that may be operating in that territory. But the problem is one that can be worked out in the same manner for other refineries. Now the Imperial Oil Refinery at Regina has cracking facilites available, so that it is possible to convert a relatively large quantity of fuel oil, which is obtained from topping Cutbank crude, into gasoline with the result that the Cutbank crude has a higher relative value in the Imperial Oil Refinery than it would have in a plant which is equipped solely for topping crude and not cracking it. Now, the way that the Turner Valley crude may be appraised relative to the Cutbank crude in Regina is then to figure out how much Turner Valley crude must be processed by this particular refinery, such as the Imperial, in order to supply the same products as the Cutbank crude is supplying. And according to Exhibit "269" and the supporting data on which - are they in, the supporting data for that?

MR. McGRATH: Mr. Cottle has them.

Q MR. FRAWLEY: I suppose Mr. Cottle has it here some place?

Dr. G. G. Brown.

A I have gone through these supporting calculations in that data and this figure is correct. That it only requires .785 barrels of 45 gravity Turner Valley crude, and about .039 barrels of absorption naphtha, to produce substantially the same products as would be obtained from one barrel of Cutbank crude. So that the cost of the Cutbank crude at Regina equal to $1.92 is going to balanced against a smaller quantity of Turner Valley crude, because Turner Valley crude has more gasoline in it and will supply the markets in a more efficient manner. However, Cutbank crude has more fuel oil in it, so that when we use a smaller amount of Turner Valley crude to supply the same markets as Cutbank, we do not have as much fuel oil left over. But this fuel oil is a low grade product. It does not bring a very good price, and there is no economic use in piling up additional fuel oil to be sold at a price below the cost of crude. So that we simply take the Turner Valley crude and produce the high grade products from it, but not so much fuel oil. But because this additional fuel oil produced from the Cutbank crude has a value, the cost of the Cutbank crude which would supply approximately the same market as this .78 of a barrel of Turner Valley crude, you reduce by 15.86 cents, which is the amount received for the extra heavy fuel oil obained from Cutbank crude. Therefore, to put Turner Valley crude on exactly the same competitive footing in Regina at the Imperial Refinery, .78 of a barrel of Turner Valley crude plus a small amount of absorption

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naphtha has a value at the Imperial Refinery of $1.77-2/10 cents, when Cutbank crude can be purchased for $1.10 at the well in Montana. From the $1.77-2/10 we then subtract the cost of the absorption naphtha as laid down at Regina, which amounts to a little over 18 cents. That is about halfway down the column on Exhibit "269", Then that leaves us $1.59-1/10 the value of .78½ of a barrel of 45 gravity Turner Valley crude laid down at Regina to be processed by the Imperial Oil Company in competition with the Cutbank crude at $1.10 at the well. Therefore, the value of 1 barrel of 45 gravity Turner Valley crude would be $2.268 at Regina. Now as I intimated there is an additional cost in the treating of Turner Valley crude due to the high mercaptan sulphur. It also has lower lead susceptibility, due mainly to the fact that there is more straight run gasoline produced and less cracked gasoline. So the additional cost for the additional chemicals and for the additional amount of lead required are then subtracted from this value of 1 barrel of 45 gravity Turner Valley crude at Regina, and we have a value of $1.96-7/10 laid down at Regina. From that we subtract the freight from Calgary to Regina of 53-2/10 cents and the loading charge at Calgary of 5 cents, and the pipe line and gathering charge of 15 cents, leaving us with a total deduction of 73-2/10 cents from the $1.96-7/10 or $1.23½ at the field, for 1 barrel of 45 gravity, Turner Valley crude. Correcting that back to 48 gravity, 2 cents per degree would add 6 cents to that, making $1.29½ cents as the price for Turner

Dr. G. G. Brown.

Valley crude in the field to put it in an equally competitive condition with Cutbank crude at the Imperial Refinery at Regina. I believe on that analysis that price is correct and it will be noted that that price is very close to the present posted price of $1.30. I would like to emphasize again that this comparison might come out entirely differently if we were making our comparison on a different operation such as a topping operation rather than a complete refinery in which topping and cracking is used. It also might be somewhat different if the marketing requirements at Regina were different, or even if the market price structure at Regina was different. But this represents a comparison on the conditions as they now exist and contemplates the production of gasoline of the same quality at Regina as at Calgary, and I believe is the best method as applied to a comparison between Turner Valley and Cutbank crude

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I might point out that if it were possible to produce a satisfactory gasoline and tractor distillate at Regina without the use of any absorption naphtha that my calculations indicate that that would enhance the relative value of Turner Valley crude by approximately 12½ cents a barrel; in that case it would be necessary to process more crude but the absoprtion naphtha could be eliminated and the crude is a cheaper material than the absorption naphtha and therefore, the operation would be more economical but I am not sure that a satisfactory product of gasoline or tractor distillate can be economically produced at Regina without the use of some absorption, however it is perhaps a matter of balancing against the actual conditions, but that would make the equivalent value of 45 gravity Turner Valley crude about $1.42. I am inclined to believe perhaps that, with the conditions as I think they exist in Montana, that even if Turner Valley crude carried a price of $1.40, that it would still supply the refinery operations at Regina; whether or not it would be used in quite such a large amount as is now used might be open to question but I believe that $1.40 would still hold to the Turner Valley crude approximately the same territory for markets that it now holds but that condition might change in a very few weeks and I do not wish to go on record as recommending any such action without much further investigation.

Q But you do ---

Q THE CHAIRMAN: What further investigation?

A A consideration of other crudes and the consideration of

[illegible]

[illegible]

[illegible]

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competition from the States in Southern Alberta, which I have not analysed here. This has been done mainly as an example to show the methods which might be used and the conclusions that would be reached from this single analysis but I do recommend as the best method of arriving at the fair price for Turner Valley crude, to proceed in this manner at other points such as Southern Alberta and any other point where it is thought that Turner Valley crude might find a market either as crude or as a finished product.

Q If the crude price were $1.40 I presume, superficially at least, one would expect to find more Montana products coming in?

A That is right and less crude run at Regina but it is just my personal opinion right now which I say might be changed with a little further study, that Cutbank crude would not displace Turner Valley in any appreciable amount at Regina if we had to pay $1.10 for Cutbank crude at the well and pay $1.40 for Turner Valley in the field at Turner Valley.

Q THE CHAIRMAN: If I understand the witnes his present view is based on the information which he now has, that $1.40 if paid the producers of crude in Turner Valley would permit of the present market being held?

A At Regina.

Q At Regina?

A I mean there might be some loss in the market at Regina but it would not be significant. Now a similar study I think should be made for Southern Alberta and we

might find there that conditions may be different there and we might lose an appreciable amount of market for finished products in Southern Alberta.

Q MR. FRAWLEY: Is there any significance attaching to the fact at the moment that the Imperial Oil is only selling products in the Southern part of Alberta by actually making disbursements to cover freight?

A Well, if Turner Valley crude is having difficulty at the present time meeting the competition of finished products from Montana crude in Southern Alberta ---

Q Yes?

A That would definitely indicate that some of these markets would have to be given up if the price paid for Turner Valley crude is increased.

Q Although the price would be increased the volume purchased at the wells in Turner Valley would probably go down and net results might be different?

A Oh yes.

Q Although, well would it, how would the comparison be there?

A Well I have not studied that Southern Alberta situation but from what you say and which I understand is correct it would indicate that my statement of $1.40 would apply only to the situation as I see it at Regina and other factors such as the meeting of the competition from Montana in Alberta itself might be a determining factor which would indicate that a price of $1.30 is about as high as it should be.

Q Yes, because --

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

Q THE CHAIRMAN: $1.40 is for 48 gravity?

A Yes.

Q As compared with $1.30?

A Yes.

MR. FRAWLEY: Ten cents difference.

THE CHAIRMAN: Yes.

Q MR. FRAWLEY: With $1.40 crude, the Montana product would penetrate further and further north, that is the difficulty, is it not, and would it not get pretty close to Calgary and lose a considerable volume to the Calgary refinery?

A I do not know how much. I have not studied that but that is a study which should be made and perhaps it is as much a marketing problem as it is a refinery problem right now.

THE CHAIRMAN: I think the witness should have a short recess.

MR. FRAWLEY: Very well.

(An adjournment of ten minutes was here taken.)

Q MR. FRAWLEY TO DR. BROWN: Now have you said everything you want to say about that Exhibit, the $1.10 Montana well price Exhibit?

A I think so if I have made myself clear.

Q Now I want to touch something else --

THE CHAIRMAN: Before you go to that, would you mind ....

MR. FRAWLEY: No.

Q THE CHAIRMAN: As I understand you, you think on the information you presently have that $1.40 field price would permit of Turner Valley

producers holding their present market, that is I say on the information you presently have?

A I did not go quite that far; I meant to say that I believe that the immediate present $1.40 at the well in Turner Valley for 48 gravity would enable the Turner Valley field to hold substantially all their markets at the Imperial Oil Company in Regina.

Q Yes?

A I do not mean to say that would necessarily leave the condition the same as the competition coming in from the States in Southern Alberta.

Q Yes. Now then I understand, yes, bearing that in mind, I understand that you feel that you should make further examination of Southern Alberta conditions before you can give a firm opinion as to this?

A Yes.

Q Because that might change the picture?

A And my present opinion is that it would. My present opinion is that any increase in Turner Valley crude would now have an almost immediate effect in the competitive conditions in Southern Alberta so that if the price of crude was raised there would be still greater difficulty in selling the finished product from Calgary in Southern Alberta and it might have an immediate effect in the loss of markets for gasoline and other finished products in Southern Alberta.

Q And it might prove in the main to be a disadvantage rather than an advantage to the producers?

A Yes, I think it would.

Q Because of what?

[illegible]

A But I was considering earlier solely the situation at Regina.

Q Yes?

A And I was going on to reach a conclusion on the Regina situation alone.

Q Yes?

A And then we can take another situation and discuss that and after you have them all before you you can then arrive at a general conclusion.

Q Yes, but what I wanted to know was, was there any evidence which could be made available to you which would assist you in coming to a conclusion with regard to the Southern Alberta situation?

A Oh yes.

THE CHAIRMAN: That of course will be made available?

MR. FRAWLEY: Yes. You see Dr. Fry is going to do that but I am very glad to have Dr. Brown's opinion on that also, and Mr. Cottle will make available to Dr. Brown any information he wants.

Q THE CHAIRMAN: And then having gotten that would there be anything else you would require in order to come to a final conclusion?

A I think those two considerations would probably be sufficient for the situation as it now exists.

Q Yes?

A I do not see the necessity of going any further.

Q MAJOR LIPSETT: I do not know, Dr. Brown, we have had some other opinions upon the subject, I do not know if you have considered at all the question of

two prices for Turner Valley crude, one say for the Calgary refinery and another for Regina and one, a lower price with a view of putting the products further East or further North?

A Yes.

Q Let us say that 90% of the product was sold at a certain posted price, where it would be possible to allow 10% of everybody's production to be marketed at a lower price, with a view of extending the market, we have had a number of opinions, perhaps you would like to express some opinion?

A That works itself out as the equivalent to an export bounty paid by the producers and the only practical way or working out such a scheme as I see it would be to organize a sort of cartel or a monopolistic corporation or group or body which would take all of the crude from all of the producers and pay them an average price and then peddle that crude out at the different prices to the different parties. It is something which I do not see, I do not see how that thing can be handled in any other way.

Q Well there may be practical difficulties but on the main question itself, have you any view as to whether such a system might be desirable or not?

A Well it would depend a great deal on what you would have to do. I am presently of the opinion that the gain in production would be obtained only at such a great sacrifice in price that it really would not be worth the effort. I believe that in order to go further East than Regina the price would have to go down very rapidly for a slight increase in market.

The freight rates are such that it works against carrying oil further East and if you try to carry it as far as Sarnia it means you would practically have to give the oil away. On the other hand, if you try to go West and carry it over the mountains and compete with California, practically the same situation exists so I believe, speaking really without a thorough study of it, but from a preliminary study only, that any such plan would really be of very little material aid in widening the market; in other words, the loss in income due to the decreased price would not compensate, would be more severe than could be compensated for by the increased volume of crude.

Q Thank you, Dr. Brown?

A But that is not final.

Q I was going to say that if anything further occurred to you as a result of your studies it would be of interest?

A I will try and study that.

Q MR. FRAWLEY: That is borne out by the Exhibit "283", that is what you have been speaking about last?

A That is an example of the case under discussion, referring to Exhibit "283", if the price at Turner Valley field price now $1.30, let us suppose that we take some of the crude and sell it for $1.25 instead of $1.30, we would gain only 63 barrels, and if we cut the price from $1.30 to $1.20 you might gain 119 barrels, and if you cut it to $1.15 you gain about 270 barrels. Well is it worth while to go through all the expense of administration and so on to gain 270

The fact [illegible] the [illegible]

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it [illegible] became [illegible] generally

[illegible] the [illegible]

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in finance due to the [illegible]

[illegible] more [illegible] that [illegible]

due to the increased [illegible].

What [illegible], Mr. [illegible]?

A Let that [illegible] not [illegible].

Q I was going to say [illegible]

to you [illegible] result [illegible]

[illegible]

A [illegible] and [illegible] that.

[illegible]. That [illegible] by the

[illegible], that [illegible]

[illegible].

Q That is [illegible] of the [illegible]

[illegible] to [illegible], [illegible]

[illegible] 1.00, [illegible]

[illegible] of the [illegible]

1.00, [illegible]

[illegible] 1.00 [illegible]

[illegible] 1.00 [illegible]

[illegible]

the [illegible]

barrels a day and then make a net return to the producers of about $1.28 instead of $1.30; in other words, you have almost reached the point where the expense involved in getting wider market more than eats up the income from the wider markets.

Q THE CHAIRMAN: That leads to the conclusion, I suppose, which has been discussed before that there is some place that you draw an economic line beyond which Turner Valley producers who produce oil should not go?

A Well.....

Q Economically?

A Yes, that is right, I think that is right.

Q Can such a line be determined?

A Yes, I think so.

Q Under existing conditions?

A I think so.

Q MR. FRAWLEY: Can you help us in that respect, of course, Dr.Fry is going to do that too, we are getting like Mr. Halverson and Mr. McGrath, but at the same time.....

THE CHAIRMAN: If this witness is competent to do it, he may do it quite differently from what Dr. Fry would, and we would have two different opinions.

MR. FRAWLEY: Well that is a point. You see I am certainly of the Chairman's opinion with respect to, that any of these matters, regardless of whether we have been leaving it more generally to Dr. Fry than to you, that any of these matters, that you have views upon and have experience in.....

THE CHAIRMAN: Where their knowledge and experience permits them to overlap, we want them to overlap.

MR. FRAWLEY: Even although they are at a disagreement, because it will help us just that much more.

THE CHAIRMAN: Certainly, we do not care where their evidence leads.

Q MR. FRAWLEY: Can you now, or perhaps when you come back, explore that a little further, where that economic line can be drawn?

A I cannot do that right now while I am on the stand, but I will do it.

Q Then we will pass from that. You stressed the fact that this price which Mr. McGrath put in and he certainly stressed it too, as to what he could pay for his operation at Regina and you mentioned that more than once?

A Yes.

Q In your statement, and another man might have quite different views as to what he could have paid for Montana crude as against Turner Valley crude and vice versa?

A Yes.

MR. FRAWLEY: And I think, Mr. Chairman, with your permission, Mr. Fowler is coming and he may be here on Monday although I think I will have him come a little later, and he will support the statement I am going to make to the witness, but I would like to get the benefit of Dr. Brown's view on it now, and I will do it in the form of a letter which I have.....

THE CHAIRMAN: Ask him to assume it.

Q MR. FRAWLEY: If you will assume with me that this will be the view of the witness Fowler, who operates the Consumers' Co-Operative Refinery at Regina, and then give me your views about it. I called, I may say, to Mr. Fowler's attention Exhibit "268", and put it to him that it seemed, without some explanation, that he should not go on paying $1.30 for 48 gravity crude at Turner Valley when it appeared that he could buy 38 gravity, if he could, if he could buy 38 gravity crude in Cutbank for $1.00.

MAJOR LIPSETT: 37.

Q MR. FRAWLEY: 37 or whatever it is, and he answered me this, and he simplybrought up the point you brought up this afternoon;

"I have your letter of May 31st, with schedule "filed by Imperial Oil in connection with the "relative value of Turner Valley and Montana "crude. I am afraid that our experie c here "is not going to be of much galue to you inthis "matter.

"Our plant is a skimming plant which, as you know, "means that we can only take out of the crude the "products as they naturally exist, and with Mon- "tana crude, with a high percentage of bottoms "and heavy fuel oil, we cannot profitably use "it in our plant at a price more than about 75¢ "per barrel. We, therefore, must use either Turner "Valley or South Texas crude.

"Another factor which enters into the value of any "particular crude in a given Refinery is the relative

"proportion of the market which that Refinery "must serve; so much percent gasoline, kerosene, distillate, etc., and it might be possible "that two Refineries, sitting side by side'

and I might interject that this Consumers' skimming plant and the Imperial Refinery are at Regina.

'one would find Turner Valley crude more profitable, and the other Montana crude more profitable, "because of the fact that the two Refineries may "have a different proportionate demand for the "various marketable products.

"We are in the midst of a Cracking Plant program "here, and when this is completed, it is quite "within the realm of possibility that we may "use some Montana crude, and it is for this "reason that we raise our strenuous objection "to a dumping duty being placed on that crude "entering this country."

I presume he means the Turner Valley producers please take note , but in any event that skimming plant man's experience is just precisely what you would expect and bears out what you have said this afternoon?

A That is perfectly sound.

Q Now I am about to leave the question of the value of crude for the time being, and it may be a good time for cross-examination on that, if any.

MR.NOLAN: There are one or two points.

THE CHAIRMAN: Before you do that, Mr. Nolan, if I might suggest to Mr.Frawley, there are

certain matters touching the Lion Oils Refinery which were referred to the other day and I observe Mr. Plotkins is here now and I wondered if you would care to deal with those now.

MR. FRAWLEY: I thought I would do it later, but we may as well do it now. I thought we might do it piecemeal, to finish up these questions, both by Mr. Nolan and Mr. Plotkins.

THE CHAIRMAN: If Mr. Plotkins is going to be here on Monday it may probably be more satisfactory, are you, Mr. Plotkins?

MR. PLOTKINS: Yes, I was sorry I couldn't be here until this afternoon.

MR. FRAWLEY: It may not be possible to get Dr. Brown away until Monday so that he can pursue these other studies, particularly as he is coming back in any event.

MR. NOLAN: I will only be three or four minutes. We might see how far we get along, and I am asking Dr. Brown to repeat what he said about that three structure the other day.

THE CHAIRMAN: I perhaps should say what is in my mind before Mr. Nolan cross-examines. The Doctor, certainly before Mr. Plotkins examines, this should be explored some more, Dr. Brown says, as I understand him, when you get up to 71 or 72, or 72 to 74 octane for ordinary cars, that speaking in a general way there is really no great need for any higher octane.

MR. FRAWLEY: Yes.

THE CHAIRMAN: Well he also says that

when you get down to third structure, since it does not consider all the products, it really is out of the picture.

MR. FRAWLEY: For this Commission's purpose in arriving at an efficient refinery.

THE CHAIRMAN: Yes.

MR. FRAWLEY: That is right.

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[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

THE CHAIRMAN: Yes and that is something in which Mr. Plotkins will have an interest and which we ourselves would like explored some more as to where that line is between the good and the bad.

Q MR. FRAWLEY: I wonder if Dr. Brown might restate that now, perhaps linking up these two ideas which do appear superficially or might appear superficially to be in conflict?

A I am just a little bit confused what you have reference to. I made the statement as I recall that we were discussing the method of determining or arriving at a fair price for the various products produced by a refinery.

Q Or even cost?

A Well all right, cost, if you will. It does not make much difference. That is arriving at the fair cost of production or producing the various products, I believe I made the statement that the consideration of a single operation which produced only third structure gasoline and fuel oil would not be the controlling factor in determining the proper price for the various products produced from crude oil for the reason that such operation was unable to supply the requirements of the community.

Q Right. That is what I understood you to say.

A That is the idea I tried to express.

Q THE CHAIRMAN: You said something more didn't you that it must then go out of the picture unless the major company keeps an umbrella over it?

A I went one step further and said such an operation which

does not supply every product required by the community and supplies only the low grade or low value products sooner or later will disappear from the operation either by adding to it adequate facilities to produce the desired products or else by folding up unless the other operations which did supply all of the materials required by the community in effect held an umbrella over such an operation so that he could get a good substantial price for his products.

Q I think that is the other statement.

Q MR. COTTLE: You added, Dr. Brown, as another proviso that unless the third structure gasoline manufacturer was able to dispose of his bottoms to another refiner who was in a position to crack them?

A Yes, which is the same thing. Unless there was some other operation that really maintained him in that position because of some other factors.

THE CHAIRMAN: That was the umbrella?

MR. FRAWLEY: Which really was the umbrella?

A Yes.

Q The market for the bottoms?

A Yes.

Q That is a pretty complete statement of what you said the other day and we restate it for Mr. Plotkins' benefit so that he can question you about it. And adding to that something which might be germane to it or which might not, your opinion today was that from your experience in studying octane numbers in these gasolines that there was no need, generally speaking, for better gasolines,

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

higher octane gasolines than the regular numbered octane gasoline, looking at the picture in an over all way?

A At the present time that is right.

Q To the extent that there is any, and there may be none, any conflict in those two statements a person like Mr. Plotkins who is a third structure manufacturer perhaps should ask you some questions?

THE CHAIRMAN: Mr. Nolan may want to ask some questions?

MR. NOLAN: Dealing with this question of the price of Turner Valley crude. As I understand it Dr. Brown, the posted field price has got two jobs of work to do, first to foster or encourage development of the particular oil field itself?

A That is right.

Q And secondly, to be of such an amount in dollars and in cents as to back up other crudes, to meet competition?

A That is right. One of those determines the high level and the other one determines the low level.

Q And a consideration of both gives you the true level?

A That is right.

Q That is speaking quite generally?

A That is true.

Q But speaking quite specifically, you know we have a posted field price of $1.30 in the Valley for 48 gravity?

A Yes.

Q Now, Dr. Brown, are you influenced in your opinion as to the correctness of that posted field price by the job of work it is doing?

A I have not considered to any extent the necessity of

developing the Turner Valley field.

Q No?

A And, therefore, I have not considered that factor in the discussion so far. I have considered solely the one factor which was the competitive condition at Regina and in the Imperial Oil Company's refinery.

Q In a word, you have considered what was contained in Exhibit "269"?

A That is correct.

Q You began in your discussion of that with a price of $1.10 at Cutbank?

A For 37 gravity.

Q For 37 gravity crude at Cutbank?

A Yes.

Q And you gave it as your explanation of your opinion that you felt that that was a reasonably low price?

A At the present time.

Q At the present time?

A For any appreciable quantity of such crude.

Q But there has been some discussion here as to how you --

A Well, let me put it this way. This Exhibit is built up on a price of $1.10 for 37 gravity crude at Cutbank?

A That is the assumption.

Q That is where we begin?

A That is right.

Q You say that is an assumption? But in your opinion --

A I think it is a fairly good assumption.

Q Dr. Brown was saying, Mr. Chairman, that while Exhibit "269" began with $1.10, that is an assumption but he says he thinks it is a good assumption, because after

[illegible] here [illegible]

[illegible] This [illegible]

[illegible] gravity [illegible]

[illegible] assumption, [illegible]

all, Dr., we cannot tell what we will have to pay for oil in an appreciable quantity.

A That is right.

Q Unless you go there and buy this oil, is that right?

A Absolutely.

Q And if you do not go down there and buy it in these quantities and observe what happens to the market by reason of your continuing purchase?

A That is right.

Q Then you do not know definitely what the price is?

A That is right.

Q All you can do is make an assumption?

A Make an assumption.

Q And give the best explanation of it that you can?

A That is right.

Q Now you said something about $1.42 that I did not quite follow. That is in my ignorance I did not follow that. Is it that Turner Valley could be worth $1.42 if we did not have to move the absorption to Regina?

A Yes.

Q What does that mean?

A If you could market at the same price as you are now marketing your regular brands of gasolines a product produced from your refinery out of Turner Valley crude without blending any absorption. Now I do not know whether that is true or not.

Q If you could?

A If you could do that.

Q Turner Valley would be worth $1.42?

A Turner Valley would then be wroth $1.42 instead of $1.29 and a half.

Q That has got nothing to do with this other figure you were good enough to give us of $1.40?

A No.

Q We disassociate those two figures completely?

A Yes.

Q Then I do understand the $1.42. Then you say $1.40 you think, as I understand you, and please correct me if I am wrong, that we might increase the Turner Valley price, the posted field price to $1.40 and not lose the market that we have. If an examination into the Southern Alberta situation reinforces that view ...

A No, I would not even go that far.

Q Oh?

A I will say insofar as the market for Turner Valley crude in Regina to the Imperial Oil Company only. I am not considering other refiners in Regina nor am I considering the Calgary situation.

Q No?

A But insofar as that one proposition alone is concerned it is my opinion with conditions as they now exist that $1.40 posted price in Turner Valley would still hold substantially all of the throughput of the Imperial refinery at Regina. I am basing that on the idea that first of all the Imperial Oil Company will be unable to get substantial amounts of Cutbank crude over any appreciable period of time for $1.10 even. I am anticipating if you go in and try and buy that crude now you might get some for $1.10 but you will find to get the balance of it the price will rise. Also that you might find you will have larger production and larger markets during the warm months of the year from Regina which will mean that you will have to blend less

absorption than has been perhaps estimated for this Exhibit "269". Now taking a combination of those factors into consideration it is my conclusion that there is enough tolerance there so that the Imperial would still continue running substantially all the Turner Valley crude at Regina under conditions as I believe they now are if the posted price were $1.40.

Q Does that involve a further study of the Southern Alberta Situation?

A I have so far excluded that. Now I also stated it is my opinion that if the price were put at $1.40 in the Turner Valley field then the Turner Valley crude would lose the markets in Southern Alberta and also perhaps somewhat in Southern Saskatchewan.

Q Yes?

A Through Regina.

Q And that would have to be considered by you, Dr. Brown, before you changed the posted field price to $1.40, if you were the person who was doing the changing?

A Yes. And other things should be considered possibly such as the one you first brought up, that is a price which would encourage development of the field at the proper rate. All of those things should be considered. But I believe that if the competition at Regina both from Illinois crude coming up from the Great Lakes and from crude coming from the Sates and the competitive situation in Southern Alberta are considered I believe any conclusion reached on those two factors alone will be substantially correct. I do not believe it is necessary to go much further in order to arrive at what should be

considered to be a proper price in the field.

Q What concerned me a little about changing the price in the field is that we automatically change, don't we, the cost of the refined products?

A Yes.

MR. FRAWLEY. Not very much though.

Q MR. NOLAN: I mean if we go from \$1.30 to \$1.40 there must be a corresponding increase in the cost of the refined products?

A Yes.

Q The selling price?

A Yes.

Q And when you talk about this \$1.40 you are speaking of the Imperial picture aren't you?

A That is right, as it now exists.

Q The Imperial picture is not the whole picture?

A No.

Q What has to be done yet so that you can make up your mind as to the propriety of the \$1.30 or \$1.40?

A In my opinion there is only one real consideration that would yet have to be given and that is the competitive situation for finished products in Southern Alberta. I believe with a further consideration of that factor we will arrive at probably the correct price, for present conditions, in Turner Valley. There are other factors which could be considered but I do not think it necessary to consider them in this particular case.

Q So that with the Imperial picture and a study, as you say, of this Southern Alberta situation, you could then arrive at a definite opinion about the \$1.40?

A Or \$1.30.

Q Or $1.30?

A Yes.

Q Just putting it quite frankly, would you change the posted field price today from what you know of the situation here?

A No. As I mentioned at least twice before I believe that any increase in the posted price in Turner Valley will have an immediate harmful effect on the market situation in Southern Alberta and my calculations, or the calculations shown in Exhibit "269" indicate $1.30 to be approximately the competitive price for Turner Valley against Cutbank crude in Regina. I feel from the study that I have made so far that $1.30 is probably the best price with the present conditions.

Q I understand that. I wanted to ask Dr. Brown one or two other questions about other parts of his evidence. Thus far we have more or less been examining on a particular point. I do not know whether you will prefer I would delay that. Will Dr. Brown be here Monday?

MR. FRAWLEY: He will be if necessary but I was hoping he would not be.

MR. NOLAN: It would only take me a moment or two.

Q If you would not mind going back Dr. Brown in your mind to what we have been discussing earlier in your evidence. You were able to ascertain from the Exhibits which were placed before you and which you had an opportunity of examining, namely Exhibit "308" (a), (b) and (c), what the spread was, and the spread as I understand you is 70.83 cents per barrel. On "308" (c)?

A That is correct.

Q In your opinion is that a fair spread?

A Yes. In my opinion I think both the spread and the operating cost and the profit as set forth on Exhibit "308" (c), which represents the conditions as they would have existed in 1938 under the present price structure, represent what would be considered a fair situation. I would like to amplify that a little bit. There is some question in the minds of some of us what the return on invested capital should be over a long period of years. And this Exhibit "308" (c) as I carried it through and referred to Exhibit "311", showed a return on capital of about 12 2/3%.

Q That is on the 1938 operation?

A That is on a hypothetical operation processing the crude they did process in 1938 and including running British American crude.

Q Quite so?

A And under the price structure as it now exists. These conditions are exceedingly favorable. As I pointed out before, the fact that the Imperial was running their plant at full capacity throughout the entire year enabled them to operate at a lower cost of manufacturing per barrel than would be the case if they had not had the British American crude. In fact I believe I stated that the cost of operating under those conditions, without processing the British American crude, would have been approximately 59 cents a barrel instead of 45.6.

Q We know we have lost the B. A. crude because they have their own refinery?

A That is right. I would like to make this point clear if I can. I have made a computation a little differently

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than that, which represents what would be the return in 1939 assuming that the markets are exactly the same as shown on Exhibit "308" (c). That is to say the price structure remains constant and during the year 1939 the British American crude was not processed and on that basis it shows an operating cost of 57½ cents per barrel instead of 45.6. That is taking into account these expenses which would be reduced by the smaller throughput and also the fact that this non-recurring figure of some twenty three thousand dollars for rental of tanks would not be included. That figures out on the same basis of a return on capital invested at the end of 1939, using the same depreciation of $283,473.00 as was used for 1938.

Q Yes?

A Of a return of 7½% on the invested capital. So that this operation and this price structure as it exists at the present time, although it would indicate a return on capital of 12 2/3% for this 1938 operation, with exactly the same conditions would indicate a return of 7½% for the year 1939.

Q That is to say, eliminating the B. A. operations and assuming the same volume --

A For the Imperial.

Q For the Imperial?

(Go to Page 9204)

So that a return of 12½% for one year, where conditions were exceedingly favourable, compared to a return of 7½% for normal throughput under the same conditions, seems to me to be a perfectly equitable return. I believe 12-2/3% is not a high return for the very reason it was not to be expected for the following year. If perhaps 12-2/3% is to be expected year after year, we might say it is a little bit high. I do not know. But I do not feel that 7½% is at all high. In fact, my opinion is in an industry of this kind somewhere between 8 and 10% certainly should be considered as a fair return. I mean a return of 8 or 10% should not be considered excessive. So that I feel this represents a fair return on the operations as conducted.

Q Yes? Then we are concerned still, aren't we, Dr. Brown, with volume? Because volume in this country as we know here depends largely upon whether there is a crop in these provinces that this Valley serves?

A Yes.

Q That, I suppose, attaches a risk or a hazard does it not to this operation?

A It does.

Q Would that influence your opinion as to the rate of return?

A That would indicate in these good years we must get a higher return in order to compensate for the small return or perhaps an actual loss that may be encountered in these years when the throughput is small, but presenting it over a long period of time, over a period of 15 years for an operation of this kind, a return of 8 to 10 per cent would certainly seem to be

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not excessive and because in one year the return of 12-2/3% is indicated, as I point out, that does not mean that the following year may be anywhere near as good.

Q As I understand it, our manufacturing costs are directly affected by the volume which goes through the refinery?

A That is right.

Q And that is the factor and that is the real factor that influences the amount of the manufacturing costs?

A That is right.

Q Because in the year when the volume of throughput is low the costs go up?

A That is right.

Q It seems to me there are two things we have in our minds. One is what was the proper return on our investment in the year that has gone by, and secondly what is the proper return which we should have in the year that is to come. Are you of the opinion that the figures with which you have been supplied by us, the historical analysis of the situation, is that what should be used in order to determine what we should have on our investment for the future?

A Well that opens up a big question and it all depends on the point of view taken. As I believe I mentioned before, a high capital investment in a plant of this kind, if it is done intelligently, results in a plant of smaller or slower depreciation. A $5,000,000.00 plant might depreciate in 20 years, and a $3,000,000.00 plant might depreciate in 10 years. So that it seems to me that it does not make a great deal of difference whether we try to look at the proposition from the

[illegible]

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standpoint of what has been done to determine what actually is the situation, or whether we wipe the slate clean and take an arbitrary position and say "This is what should be done." I think we would come out with just about the same answer.

Q You say if you take a high capital investment and a low depreciation, you are going to come to the same result as if you had a low capital investment with a high depreciation?

A Yes, in most cases. I believe that is true here.

Q Do you think that we can safely go ahead on our historical study as obtained from our books to fix a price which will be in effect in the future, or do you think there should be an appraisal? Fix a rate which should be in effect in the future or should there be an appraisal made of the assets there?

A Well I am a little bit confused as to the purpose of this. If you were the only refinery in Calgary and were supplying all of the gasoline and other products used in Alberta, I believe there would be a perfectly sound argument, perhaps, for saying the Imperial is, to all intents and purposes, a public utility and should be subject to regulation, because they have a monopoly.

Q That being the basis of public utilities. Monopoly being the basis?

A Oh yes.

Q Exclusive franchise?

A Yes.

Q Yes, all right?

A Now, is that is the case, which I believe is not true,

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we then approach that from one angle. If we take the situation as it is in which there are two, three or four operations, or perhaps more supplying the markets in Alberta, I do not see that any appraisal or any consideration of even your historical depreciation is going to be a deciding factor.

Q What is?

A It seems to me under those conditions that that particular operation which can supply the requirements of the community at the lowest cost or the lowest price, should be regarded as the controlling factor, and that particular unit operating in conjunction with the others which are in existence.

Q That is the lowest refining costs that you spoke about earlier in your evidence?

A Yes, under conditions as they exist.

Q You take that as a yardstick?

A I believe that would be the proper basis under these conditions.

Q And not an appraised value?

A No, not under these conditions as they now exist here.

Q You do not think the conditions as they exist here lend themselves to public utility regulation?

A No.

Q I wonder if the fact that the products of this refinery are distributed in three Provinces has led you to that conclusion or influenced you?

A No, I was not considering it from that standpoint.

Q But if you did consider it?

A That would only complicate the public utility attitude. It would mean that that utility would have to be

controlled perhaps by a Board common to the three Provinces.

Q You said something when you were being asked about those octane gasolines about the luxuries of today being the needs of tomorrow, Dr. Brown, and you did not go on and explain that in any way. You have an explanation I am sure of what you mean by that remark? It arose out of Mr. Frawley's observation that there was a race, an octane race between refiners. Is that your opinion that there is an octane race between refiners?

A Yes, that is true. There is also a race between the motor car manufacturers to put out the fastest and most powerful and most attractive automobile.

Q Is the refiner trying to keep up with the motor car or is the motor car keeping up with the refiner?

A They are both trying to keep ahead of each other.

Q MR. FRAWLEY: Which came first, the high compression motor or the high octane gasoline?

A Which came first, the chicken or the axe? I did not mean to be facetious. In actual practice the condition seems to be that the motor car manufacturer will produce a car requiring high octane fuel only when he is sure that that car will be able to obtain that high octane fuel, and the refiner on the other hand figures if he can market a higher octane fuel, or a premium high octane fuel, he will get the cream of the market. So that the two of them, not working in cahoots.

MR. FRAWLEY: Perish the thought.

A Far from it. The two of them pushing at the opposite ends of this condition just up the whole structure.

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For example, there are cars now being manufactured, which as I said before will operate satisfactorily with the regular grade gasoline. But these same cars, by a change in adjustment will gain in performance by certain critical conditions by the use of premium or Ethyl gasoline. If the gasoline is universally available these car users may adjust their cars to require that particular fuel. Then what happens is this, the refiners say "Here is a car I cannot service with my regular gasoline," so he ups the regular gasoline, putting it on a par with the old Premium gasoline and he advertises "our regular gasoline is as good as any on the market". There is a lot of that being done repeatedly. There is no use paying a premium for Eth'l, that is the way it is spelled frequently, because his gasoline is just as good. Then the motor car manufacturer says "Well, I can use a regular gasoline in this car with a high compression ratio, and so all of these cars can be adjusted for the higher octane. That has been the history and indications are that that same condition still exists. It is not the motor car forcing the hands of the refiners any more than one refiner forcing the hands of any other refiner.

Q It is just the march of progress?

A It is the march of progress under a competitive situation. If there was no competition the condition would not exist.

Q Thank you, Doctor.

THE CHAIRMAN: I suppose it is not

generally known that when you buy a motor car you should make up your mind what kind of gasoline you are going to use and have it adjusted accordingly?

A That is right.

Q That is, you cannot have third structure one day and Ethyl the next?

A No, not and get the benefit of the Ethyl.

MR. FRAWLEY: Well, we have Mr. Plotkins now.

Q MR. PLOTKINS: Dr. Brown, in the opening of your evidence you gave as one of the considerations in fixing the price in Turner Valley the need for considering development and markets as a whole. That is you painted a picture in the United States where you said, as I recall it, the price is calculated to not only make available these products for our present needs but to maintain reserves, at least maintain conditions that will permit of bringing into play reserves for the future.

A I did not put it that the price was calculated on that basis, so much. I wished to state that that was the basic idea over a long period of time covering the entire United States as the guide in indicating what was the proper price. But insofar as the petroleum Conservation Board at Washington or any other body sitting down and figuring out a price and posting it, no such thing happened.

Q What you implied was that the price must of necessity be sufficient to provide not only for present production needs, but must include, at least the industry must as a whole provide funds in that price to permit exploration

work?

A That is right.

Q Now when you made that remark you had a definite picture or a definite situation in mind, that is the United States?

A Yes, I said in the aggregate over a large area covering a number of fields over a relatively long period of time such as fifteen years.

Q The reason you used the United States is because it is an entity insofar as market is concerned.

A No, because the United States covers a large area and has a number of fields in it and its petroleum production experience extends over more than fifteen years.

Q And the crude market available for one field is also available to another field in the United States?

A Well the same as between Montana and Alberta, yes.

Q But there is this distinction, that whereas between Montana and Alberta there is a line, the International Boundary, and there are complications in the form of tariffs, there are no such complications as between the States, is that not a fact?

A No. We have had ports of entry at various States' border lines down there, with different taxes on the gasoline in one State than in the other. It has gotten to be a highly confused condition in many places. But I do not quite follow your question. But if you are trying to indicate that because there is an import duty on the finished product, is that right,....

Q No. What I wanted to point out to you is, the United

States' oil industry tries to provide for its own needs for national needs and that because there is no duty on crude between the States competitive conditions can have their full play and the industry in the United States is justified in taking into consideration only factors that affect their home market. Whereas in Canada we have not got sufficient crude to supply our needs and we may be justified in using some other factor in establishing the oil industry here.

A Is that a question or a statement?

Q No, it is only to ask you this same question. Is the situation in the United States similar to the situation in Canada with respect to the needs of providing funds for future development and for present requirements of crude.

THE CHAIRMAN: Out of the return allowed on the capital invested?

Q MR. PLOTKINS: No. Only with a view to bringing out the fact that here we have the first oil field which only supplies a limited market in Canada. If we can encourage by a price situation, as they do in the United States, and which Dr, Brown says is one of the factors considered, if we can encourage in the price structure sufficient funds or make available to the producers in Turner Valley or elsewhere by price calculations, to provide sufficient funds, then we will discover other oil fields and gradually there will be a Canadian industry placing itself or taking into consideration the same factors that the American oil industry does,

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and we won't be tied to the American situation such as we are today. We are trying to relate Montana crude to Alberta crude, whereas we have an International line. We have a tariff on finished products. We have other conditions that militate in favour of Turner Valley crude, and I am going to suggest to this witness that we may be well advised in considering the Turner Valley situation on a Canadian basis as distinct from an American basis.

(Go to Page 9214).

WITNESS: I think I understand you, I am not sure, your position is that the high price in Turner Valley will encourage rapid development of the field, perhaps at such a rate that Turner Valley might produce sufficient crude to supply Canada.

Q No, that is not it. I am only referring as to policy; its application may not be quite so strong or quite so violent as what you have just suggested but the principle that you have just told us of, that is applied in the United States by the oil industry as a whole, why cannot that same principle be the governing factor here for the Commission to take into consideration in arriving at what is the fair price in Turner Valley for crude oil?

A I think it should be, but you have not said more than a very small part of the consideration. As I stated a few minutes ago, I stated that over a long period of time, over a large area, where there are a number of fields, the basis for consideration should be that the price should be set so as to encourage exploration at a rate which would maintain reserves of approximately 15 years, but I immediately departed from that and I said from a practical consideration the same result is obtained by considering the competition between the various crude producing territories, because if we consider how one territory bucks against another one, one producing field pushes another one back, we get the whole thing in balance, and then to see whether or not the average composite crude price, that is the only thing that we were talking about, in the long period of time is proper. We may check

[illegible]

back and see if we maintain 15 years' reserve but that is of no use whatsoever in trying to determine the price in one field. That policy is of practical utility only in determining the average over-all price levels for a whole continent or perhaps for the world, but it cannot be applied to any smaller area than that and the only way to handle the situation that we are faced with here, where we have only one particular area, is to consider that field in relationship to the other fields with which it will come into competition at certain points.

Q You mean there, are we to conclude from what you have just said that if the competition from Montana or elsewhere does not permit profitable development in Turner Valley, that we should just close down the field, should we?

A No sir, I did not, it means if that is true you should put a tariff on crude into the Province.

Q A tariff on crude?

A Yes.

Q At the present time, as you know, Dr. Brown, there is a tariff on refined products?

A But none on crude.

Q None on crude?

A Allright.

Q You have told us a little while ago that in your opinion Cutbank crude could not come into Regina and I gather that you implied also into the Calgary Refinery of the Imperial Oil at the present time on the basis of $1.10?

A No, I said that if Cutbank 37 gravity crude could be purchased in adequate quantities to keep, say for

[illegible]

example, a specific area, the Imperial Refinery at Regina, supplied, that the competitive position of Turner Valley crude would justify a price in the Turner Valley field of $1.29½ for 48 gravity.

Q Yes, but what I am asking you about now, Dr. Brown, is this, you say the only way that we can favour the Turner Valley field in the face of competition from other fields?

A Yes?

Q To permit us to develop it would be by a tariff on crude?

A No, no, I didn't say that at all.

Q I misunderstood you.

A What I said first, and I will try and make myself clear, is that in the long range over a wide territory, considering perhaps the entire American Continent, it is an opinion, that the price paid for crude must be such as to encourage development of all of the fields, but that that policy, that philosophy, is of no practical use in trying to determine the proper price for a particular situation as it exists in Turner Valley. That, it was my opinion, that the best way of arriving at the proper price for Turner Valley crude was to consider its competitive situation or position in relation to other crudes and the products from other crudes at various specific points, and under certain specific conditions.

Q So that you do not agree with the contention that we can treat the Turner Valley field on a Canadian basis in arriving at the market value for the crude, which would permit of the development, not only in Turner Valley,

but in other particular fields in Canada?

A I do not know what you mean by "Canadian basis". It is in Canada and it is in Alberta, and I have considered it from the standpoint that it is in Alberta and, therefore, it is on a Canadian basis.

Q But you have considered it in relation to the American oil fields at Cutbank?

A Certainly, because the American oil fields are also present. If there was no crude oil on the American Continent except Turner Valley crude, I think we would be attacking this from an entirely different position, but that position does not exist and I do not think there is any use in looking at it from that particular standpoint.

Q No, but as I understand you, Dr. Brown, you were quite definite, that there was not sufficient crude available in Cutbank to supply the Imperial Refineries at Calgary and Regina except by raising the price in Cutbank, in other words, if tomorrow Cutbank, I mean the Regina and Calgary plants were to seek for crude in Cutbank, your opinion was that they could not purchase all their requirements at $1.10, is that correct?

A The last statement is true but I do not subscribe to the former part of it, but the last part of it is exactly what I stated.

Q All right. Now then if that price, if the Imperial could not purchase at $1.10 then it seems that we can raise the price of Turner Valley crude at the field?

A That is exactly what I said.

Q All right?

A But now wait a minute, limiting that, do not forget,

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to the particular situation only, of the Imperial Oil Refinery as it is now operated at Regina, I stated it as my opinion that the price in Turner Valley could then be $1.40 but that was not considering the competitive situation in Alberta.

Q Yes, I am going to come to that later on, that is a further position?

A My position at the present time is that considering the Regina situation alone, excluding all else, that $1.40 for 48 gravity Turner Valley crude in the field would still enable Turner Valley to supply the requirements of the Imperial Oil Refinery at Regina, and that is based on considering a number of variables which are subject to very rapid change.

(Go to Page 9219-).

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[illegible]

Q Now, coming to this Southern Alberta situation which has been described, are you familiar with the actual competitive situation that exists in the sale of refined products?

A Where?

Q In the Southern Alberta district?

A No.

Q You are not?

A No.

Q Well now.......?

A I have made only a preliminary study of that.

Q I am going to make a suggestion to you for the purposes of your giving us your opinion on it, at the present time, the reason that Montana refined products enter Southern Alberta and Southern Saskatchewan is because the marketers, that is, the independent marketers, you know it is not being brought in by the Imperial Oil, from Montana, into Alberta or into Saskatchewan?

A That is my understanding.

Q Or not the British American?

A That is also my understanding.

Q That is not the major companies, in other words?

A Those two statements you have made, my understanding is, that the British American is not bringing in any products across the border into Alberta nor into Saskatchewan, and the same statement applies to the Imperial, that is my understanding.

Q The Texas Company does?

A That is also my understanding, yes.

Q Well, now, apart from the Texas Company, the situation is that the products, the refined products, are brought into

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Alberta by the independent marketers and those independent marketers work, that is, merchandise their purchases that they have made in Montana from Montana refineries on a lower spread, marketing spread, than the Imperial or the British American chooses to make on their products?

A Now, you are getting into the marketing situation and I have studied that in Alberta only very briefly because when Mr. Frawley came to see me he asked me to to into the refinery situation and also study the relationship of the various, of the factors which determine crude prices, and he told me that I would not have to study the marketing situation as he was employing Mr. Fry to do that, so now you are getting outside of any statement which I have made so far before this Commission, and I do not believe that at the present time I am competent to discuss with you marketing spreads or anything of that nature.

Q No, but you have said you would want further study of the Southern Alberta situation before you could say what in your opinion should be the fair price for Turner Valley crude?

A Not quite that way. I said that it was my opinion, based on the limited study which I had made, that any increase in Turner Valley crude would have an immediate affect on the quantitiy of finished products marketed in Southern Alberta produced from Turner Valley crude in Calgary.

Q Yes?

A Or if it did not have an effect on the quantity, it would certainly have an effect on the income of the refiners.

refiners and the marketers.

Q Yes, but as I understand you, you were trying to point out, if you raise the price of crude, there would be more products come into Southern Alberta?

A Or else less money made by the marketers and the refiners.

Q Oh yes. Now that is a different matter, making a little less money, but what I am trying to get now, to explore, is the question of more products coming in?

A Well that is a question of marketing, and I wish to again state I have not made a thorough study of the marketing situation, and have not discussed it so far, and I do not think I am competent to discuss that with you.

Q I am going to ask you, Dr. Brown, just to assume that that is the situation, for the purposes of this question.....

THE CHAIRMAN: Mr. Plotkins, I suppose you will be taking some time, I do not wish to shorten your examination at all, but what would you expect, roughly, an hour?

MR. PLOTKINS: Oh, possibly thirty minutes, roughly.

MR. FRAWLEY: Just on the last point, Dr. Fry will be going very fully into that, and Mr. Halverson, of course, but your point is it ties in to some extent with Dr. Brown.

MR. PLOTKINS: Yes, I do not see how the Marketing Department can tell me what I want to know.

WITNESS: Perhaps I misunderstood what he was getting at.

THE CHAIRMAN: It is going to take some time,

Mr. Frawley, and I do not think the witness should be asked to stand all day and long into the night, but yet he must be fully cross-examined. I think we might as well make up our mind that we should let it go over until tomorrow, if Dr. Brown wishes to get away tomorrow night.

MR. FRAWLEY: Yes, that is my position.

THE CHAIRMAN: I understand you have already made an appointment for the witness with respect to the B. A. plant.

MR. FRAWLEY: Yes, for the morning. The hour has not been fixed, but some time in the morning. The more of the morning down there the better, I would think, for the witness.

WITNESS: I am willing to stay here longer if you wish.

THE CHAIRMAN: Would 2:00 o'clock tomorrow afternoon suit you?

WITNESS: I am willing to continue to suit your convenience.

THE CHAIRMAN: Well, Mr.Plotkins, like all other cross-examiners, when he says half an hour, he is probably going to be an hour or more, and in that respect he is like most legal cross examiners, we never know just how long we will be when we make our estimates. All right, 2:00 o'clock tomorrow afternoon.

(The Inquiry was here adjourned to be resumed at 2:00 p. m. June 17th, 1939)

The Province of Alberta

IN THE MATTER OF THE PUBLIC INQUIRIES ACT

—and—

IN THE MATTER OF a Commission, dated the 12th day of October, A.D. 1938, to inquire into matters connected with Petroleum and Petroleum Products

Commissioners:

The Honourable MR. JUSTICE McGILLIVRAY
(Chairman)

—and—

L. R. LIPSETT, ESQ.

Session:

CALGARY, Alberta JUNE 17th, 1939

VOLUME 80

I N D E X

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DR. G. G. BROWN, having been recalled.

Q THE CHAIRMAN: I wonder before Mr. Plotkins proceeds if I might bother you, Dr. Brown, to just repeat to the extent that it is repitition that which you have said about, not what you have said about the suggested field price but rather how you would approach getting at the field price, supposing you were the dominating figure in say the Imperial Oil Company that does post the field price in Turner Valley and you wanted to arrive at a field price that was fair alike to your company and to the producers of crude oil and which gave recognition to the realities of competition or any thing that should be taken into account, how would you go about setting that price, what factors would you take into account, what evidence would you marshal before you to arrive at it, could you just clear my mind about that, I am a little vague and confused as to what you have told us?

A Well the procedure that I would follow under those conditions would be to make up my mind first of all that we wanted to run Turner Valley crude at Calgary and at Regina to be specific---

Q Yes?

A And that we wanted to supply the markets in Alberta a East through the regular Regina territory.

Q Yes?

A And probably carry the products from the Regina refinery as far East as would be desirable to insure the Regina refinery operating at a fair rate of capacity.

Q Yes?

A And then consider what the price back in Turner Valley for

Turner Valley crude would be that would enable the Imperial Oil Company to use that Turner Valley crude and supply this territory on a basis so that they would not lose any money by doing that as compared with taking some other crude at Sarnia and shipping it up from Sarnia or from buying some crude at Cut Bank in Montana and bringing that in and refining that and then secondly I would have to check that competition to see whether or not there might be some finished product that would be shipped in from the United States and to Southern Alberta or possibly around from the Pacific Coast, that would undercut this Turner Valley crude price as determined in that manner and if I found that the Turner Valley crude could be processed at Regina and keep the plant at Regina operating at its proper capacity and could be processed in Calgary and the Calgary refinery then supplying substantially all of Alberta except for perhaps a few miles at the Southern extremity, it would then indicate that I had reached the proper price for Turner Valley crude. Now I consider that that method automatically takes into consideration the other factors which I have discussed briefly yesterday; in other words that automatically puts Turner Valley crude into its proper picture in terms of crude production really throughout the world because it is possible of course to bring in crude from Venezuela up the St. Lawrence, refine it and bring the refined product up through the Great Lakes and then bring those this far West under certain conditions but what holds that Venezuela crude back is the crude that comes up from Illinois and the Mid-Continent so that if we consider the Turner Valley crude in Turner Valley in Alberta and in Regina in that way we have really at the same time con-

sidered the world picture so I really believe that there is no use at all in being concerned with the whole world structure as to the price of crude but simply consider Turner Valley as a local situation existing in the world picture.

Q Yes?

A And as soon as we get Turner Valley in balance with the other crude that might compete with it then we have it in balance with the world picture.

Q That is to say, and I am only repeating so that you may correct me if I am getting the wrong understanding, that is to say that the Imperial have two refineries, as you have said?

A Yes.

Q It is to be considered then that they will buy crude oil somewhere?

A Yes.

Q To put through their refineries, to make use of that capital expenditure which they have invested in these two plants?

A Yes.

Q And they then in determining what they will pay for Turner Valley crude, look to see what they can get crude for from elsewhere that will serve that particular region that they must serve with those refineries in order to have those refineries operating at a capacity which will justify their expensé?

A That is right.

Q And so really it boils down then to what they are justified in paying in the light of what they can get crude for elsewhere?

A That is right, that is the first item.

Q That is the first factor?

A Yes, and the second one----

Q Is?

A Is to arrive at that same competitive balance through the finished product.

Q Yes, that may oust their finished product?

A Correct.

Q Unless they can buy their crude at a certain price?

A Yes.

Q That is to say, having gotten the crude more cheaply from Illinois or Cutbank they say "we do not need your crude"; But they also are concerned that they should not carry on their refining operations at a loss in that other refined products may be sold in that region and undermine them and they have nothing but a lot of goods on hand which they must sell either at a loss or store at a loss?

A Yes, in other words the competition between Cutbank crude was considered here yesterday.

Q Yes, quite so?

A At Regina but we did not consider yesterday the competition between the finished product from the American refineries in Montana coming into Alberta nor did we consider yesterday the competition between the finished products of Illinois crude or some other crude coming up from Sarnia or from some other refinery perhaps in the States.

Q Yes?

A And I mentioned yesterday that considering only the competition with the Cutbank crude at Regina it would appear----

Q Oh yes?

A That $1.40 might be paid.

Q I quite understand that before giving any firm or final

opinion there are factors which you want to look into?

A Yes.

Q But I am just now concerning myself with the approach, the method to be applied, whatever results you may arrive at, having examined into the features that you are not now familiar with, so does it boil down then to this that we, as Commissioners, ultimately must say that in answering the question "What is the cost, the proper cost of the production of crude oil", that we make such answer as we can on the evidence but having made it, maybe we will have to say that we do not know, no one can tell us, it may be that we will have to say that, but to come to your end of it as I am understanding you now, we will certainly have to say that the cost of crude oil, if ascertained in anywise, has a bearing upon the field price of crude oil which it is right that the present posting of the price, that the buyer posting the price, should post?

A I think they are entirely separate considerations?

Q Unrelated?

A Yes.

Q I want to be clear about that, in most things when you are buying something you ask "well what does it cost to produce it", there is some relation?

A Yes.

Q But in this case it is just a matter as I am understanding you, of what is the competitive situation whether in respect of crude or the refined product?

A And the territory that you want to serve fixes the competitive conditions.

Q Yes, yes, that . fixes the area?

A That is right.

Q Because your refineries to operate advantageously must cover certain territories?

A Yes.

Q They must have certain volumes?

A Yes.

Q I think I understand that and it does not matter what the producer can produce for if he wants to sell his oil he has to sell it at a price which has to meet the competitive situation?

A Right.

(Go to number 9229)

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Q Then again, not wanting any figures out of it, but is not our situation this, that we have to find where is the competition, from whom?

A That is right.

Q Which Turner Valley has to face?

A That is right.

Q And (2), if it is true competition?

A Well yes, you have to find the competition. It is somewhere.

Q Yes, and you have to find where it is?

A Yes, of course.

Q Now, it has been suggested in the course of evidence here, and something you might not want to explore, that you may not feel competent to explore, I mean, you may not have the necessary information, but we have the concrete suggestion made to us that competition is a theoretical rather than a real competition in America, including Canada?

A On crude oil?

Q On crude oil, on everything in connection with the oil business, and it should be explored at some time by somebody competent to speak, that there is economic domination through the heads of great corporations, that the seemingly frantic competition amongst those in subordinate companies and in lesser positions is very real so far as they are concerned, but that at the top there is complete harmony and agreement as to what should be done, do you feel competent to express any opinion about that from your actual experience and knowledge, however obtained??

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A Well, I think I can state that there is, there can be no doubt when the whole area of the United States at least is considered, but what there is a very real competition in the production of crude, and the refining of crude, and in the marketing of the finished product. I have been pretty close to the refining and fairly close to the marketing problems for, oh, perhaps 15 years, and there is not a bit of doubt in my mind but that that competition is very real.

Q And in connection with the purchase of crude, would you say the same?

A Yes, considering the whole area. Of course, there are certain gathering systems owned by one company in a certain field, and that gathering system will control the price of crude which is delivered to that gathering system, but in more than one case, I have seen other producers break away and put in their own gathering system, their own pipe-line, to get an entirely separate outlet for their crude oil, that has happened in Michigan in a number of cases, and of course with one company going into a field with its gathering system and no other purchaser for crude in that field but that one company, if the field develops very rapidly, there may be more crude available than that one company can take, and then I have seen, many times, an independent gathering system constructed in order that crude independently and in competition with the original gathering system will find a market.

Q Well, I just want to clear the issues, if one may call them that, although there are none strictly speaking here,

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I think it is quite clear, Mr. Frawley, that according to the evidence of this witness that so far as the field price goes, we are concerned with the competitive feature, stated in the fashion the witness has, plus a determination of the realizations of the competitive situation, so far as the evidence of this witness goes that is where we are left.

MR. FRAWLEY: Quite.

THE CHAIRMAN: Well, with regard to the producer in the Valley, it cannot matter at all whether he is producing every barrel at a loss, Dr. Brown, and it just occurs to me, and may I put it to you that if, if the price paid is so low that producers cannot possibly continue to exist, might it not be to the disadvantage of the refineries already erected that the oil field would go out of business pro tem, at least, or is the answer that it will not, it need not matter to them from an economic standpoint in any event, so long as they can get their crude elsewhere?

A Well, let us suppose, I talk in figures, it is rather hard for me to get away from it, let us suppose that the price of $1.30 which is now posted is not sufficient to pay the drillers and the producers for their effort in bringing that oil to the surface, in other words, they are producing at a loss.

Q Yes?

A In the long run, it would develop that the amount of oil produced would decrease.

Q Yes?

[illegible]

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A Because there would be no further drilling and no further development.

Q Yes?

A With the result that the crude oil would no longer need to seek a market at Regina, for example; it would then lose its more remote territory and supply only refineries at Calgary and these refineries at Calgary would then supply only the territory that they can supply at the higher price for crude, in competition with the other fields, and then there would be a new equilibrium reached with the price of crude at perhaps $1.50 which would reimburse the producers of crude, and put that crude in its proper competitive situation; in fact, I think that is nothing but retracing history. If we would go back from the present into the past, we find that as the crude price was higher than it now is, that the actualy territory supplied by that crude was less and in order to take on a wider territory and to strike, so to speak, an equilibrium at a reduction of perhaps 25,000 barrels, it was necessary that the price of the crude in the field had to be reduced so as to strike that new balance.

Q Speaking of the Imperial now only, because we are personally dealing with their account, if the Imperial had only the Calgary refinery, for example, while through the medium of that refinery, they would perhaps have a smaller zone, but it would mean that a less number of producers would get more for their oil?

A More per barrel.

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Q More per barrel?

A That is right.

Q Yes, and so far as, leaving aside the field price just now and turning our minds to the producer, if I am understanding you aright, what any Commission concerned with making answers about producers will have to have in mind is where is the economic line from the producer's standpoint?

A That is right.

Q And whatever conditions there may arise as to ascertaining what is the true operating cost in the sense of amortizing?

A Yes.

Q It ought to be possible to ascertain what is the true operating cost per well, of the going well, with a deduction for depreciation, which may be only an intelligent guess?

A Well, if we assume that that can be done, that is possible, I do not know whether it is in this case or not, I have not studied it.

Q No?

A But if that could be done.

Q A petroleum engineer should be able to tell, or hould he not, the operating cost of a well of a certain depth under certain conditions?

A You mean actually running?

Q Yes?

A Oh, yes.

Q I mean a man may not get full depreciation and will continue to run, that is what I am thinking about, providing he is not losing money in dollars every day he is running?

A That is right.

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Q He may lose his capital?

A That is right.

Q But I suppose if he makes a profit on operations?

A That is right.

Q He is liable to continue?

A He will continue.

Q Yes, but the minute you reach the stage where he is at an operating loss all the time, he would stop, would he not?

A Yes.

Well now, if that figure could be determined, it would appear to me that the next consideration would be what is the economic territory that the Turner Valley crude could supply?

Q Yes, yes?

A So that the competitive price will be adequate and sufficient to continue developing that particular field.

Q Yes?

A And if we happen to get along on that and guess on too wide a market and too low a price in the field, the field will not be developed.

Q Yes?

A Well, if we are too conservative the other way, and guess at too small a territory, the price would be a little high and the field may develop very rapidly and there would be a large amount of crude seeking a market and that would again force a wider territory and bring about a decrease in posted prices.

Q Yes, so, yes, then we have been told about the advantages of proration amongst people, amongst the producers, with

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a view to conservation?

A Yes.

Q Of this great natural resource?

A Yes.

Q Do you think it should involve control of the number of wells drilled to prevent that situation you have last alluded to?

A Well, the only way to develop the field is to keep on drilling; as soon as drilling ceases, then there is no further development.

Q If you are able to establish the economic line, you would not believe in drilling to a greater extent, at least drilling to the extent that would produce oil beyond that which is necessary to go out up to that economic line, would you?

A Supposing we have the economic territory determined for the present conditions, and in order to supply that territory, there should be in the ground proven reserves to last for a certain number of years......

Q At a given rate of withdrawal?

A At a given rate of withdrawal. Now, let us take the figure of say 15 years, that of course would depend on other factors, but that would seem to be a fair figure.

Q Yes?

A That crude is withdrawn from the field, the present reserves will decrease corresponding to the rate with which the crude is withdrawn; in order to continue having in the field proven reserves for 15 years, it is necessary that we prove the territory at a rate equal

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to the rate of withdrawal.

Q That is right?

A Therefore, there must be continued drilling.

Q Oh, surely?

A And the continued drilling will of course depend upon how much production is provided by each well or each hole which is drilled.

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Q But does not one go to keep continued drilling in line with the continued drop in production of existing wells, and having established an economic line that would be the ideal thing to do would it not?

A That is right.

Q And that being so, I am saying do you think that should be the subject of control, if there is an economic line and it is ascertainable, then as I understand you the drilling to be allowed, to have an ideal situation, would be drilling that would be comparable with the reduction in the existing wells, which is to be expected?

A Yes.

Q So as to keep a proper level that you may always reach your economic line but that you may not have a surplus which will force you beyond the economic line and force down the price of crude as a whole. What I am coming to, and it is something that has been suggested inferentially at least, and we should explore it, do you think a Board should be set up to take some control of this, or just let it go on and let everybody drill that can regardless of how much surplus oil we have and what we sell it for? And when I say a Board it won't be this Board. Do you think there is sense in it or is it something that should only be mentioned to be discarded? Or perhaps you would like to think about it before answering? These are all things we have to worry about?

A My mind is very open on that particular question,

because when you are dealing with mineral resources, be they coal or oil or anything, these resources are at least to a certain extent burdened with public interest because they are irreplaceable.

Q Yes?

A And that is a question which I think would demand very thorough consideration. I frankly do not believe I had better start in on that this afternoon.

Q Very good?

A The only thing I would like to point out at this time is that perhaps drillers in the field have an idea that they can expand their markets and serve a territory beyond the Regina and Alberta territories, and might even go further East and might even have an idea they could get down to the Pacific Ocean. Whether or not their ideas are sound I am not concerned with. But if they are to try out their ideas in practice it would follow that they must be allowed to drill at any rate they choose so as to prove up the field. Because it will be impossible to extend the markets much further than they now are unless Turner Valley has, or rather unless this Province of Alberta has proven much greater reserves than it now has.

Q That is right?

A So that whenever that control is considered at the same time we must also consider whether or not we would want to limit the markets supplied by this crude. Because as soon as that control is super-imposed on the drilling, that control will be super-imposed on the basis and with the inevitable

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result that the markets for the crude will be limited to a certain territory.

Q That is right. Now that is one of the things. And when I say anything that you would rather not enter upon now, I hope you will feel free to say so. One of the considerations we have to face, we have to face all these fundamentals and no amount of detail will get us away from the fundamentals. We have to find just such a thing as that. What is wise? We know all about us there is a cry for wider markets and it is our job as we appreciate it to quite disregard that if it is economically unsound in making our recommendation. If there is an economic line beyond which the producers can only go at a loss, it is our duty to say so. Well, thank you, Doctor. There are some things I have mentioned to you today only because I want to think about your answers while you are away. I am afraid, Mr.Shaw, I have taken the time that you could have well used because owing to the death of a distinguished Member of the Bar we are going to rise at a quarter to four o'clock. I should add to that the members of this Board, as I am sure every member of the Bar, will greatly regret. Now I am saying that about the time so that you may know all the time you have with this witness. I would not have taken the time from you for my questions except as I say I wanted to think during the adjournmant of what Dr. Brown had to say.

MR. SHAW: It is an interesting and informative discussion. I have only one or two questions that I want to ask, and Mr. Plotkins has been investi-

gating a particular matter and wants to ask him some special questions on it. But if I may be permitted I would like to ask one or two questions at this time.

Q Doctor, I gather from the newspapers and otherwise that you are the head of the Oil Research Department of the University of Michigan?

A Well the University of Michigan has no Oil Research Department. I am in the Engineering College in the Department of Chemical Engineering and within that Department all of the petroleum work is done, and I have been in charge of that work for fifteen years.

Q Now, Doctor, does fifteen years represent the life of that particular Department or subdivision that you are in charge of at the University?

A I hope not.

Q It has been going on previously has it?

A Well, Professor Leslie was there from 1920, and he was very active in that field for about five years.

Q Another question, is there any oil well drilling or any producing of oil in the State of Michigan?

A Yes.

Q And of course there will be considerable refining?

A Yes, there is some refining there.

Q You are engaged, I take it, in training students for specialised work in connection with this petroleum work?

A Yes, a good proportion of our students go into the petroleum industry. I teach other work than petroleum.

Q I want to get, very frankly, I want to see if your

experience there could be of any value to us in training students in our University for petroleum work within our field, which we hope will extend, perhaps, the more optimistic of us hope will extend beyond the confines of Turner Valley. We are interested in training our own men if we can, and fit them for that scientific work. I was wondering if you could give us anything of your experience that would be of value in regard to these matters.

A What is it you wish me to do, to set forth the philosophy of education or something?

Q Oh not at all. I want you to think only in the terms of petroleum engineering. You have that Department in the University of which you are in charge. Now we haven't any such thing, as I understand it. It is a branch of chemical engineering?

A It is at the University of Michigan, yes. Other places it is not.

Q Have you any means of support for that variety of work, financial means, I mean, other than from the University itself?

A No.

Q It, too, is a State University?

A Yes. Occasionally there are Fellowships that are supplied by various industrial companies, in the petroleum field and other fields for special research work, but the Department is maintained by the State.

Q It is paid for out of public funds?

A Yes, and the tuition and other things.

Q Now, Doctor, in your experience I assume you have found that a very valuable means of training students for this particular variety of work, have you?

A You mean the University?

Q Yes?

A Yes, we have a rather good reputation there, I believe.

Q Is similar work carried on in many other Universities, take in some States which are perhaps more concerned about the production of oil and the refining of it than Michigan?

A Yes, the State of Texas has a number of Departments of Petroleum Engineering, mainly production of petroleum rather than refining. And the University of Oklahoma has a Department of Petroleum Engineering, which is production. There the refinery engineering is in the Department of Chemical Engineering. You can enumerate them in many States.

Q That is a branch of University work that has been developed in the last fifteen or twenty years, has it not, or has it?

A You mean petroleum?

Q Yes? The matter of training students for the scientific work involved in the petroleum engineering phases of all kinds.

A It has expanded very greatly I would say during the past ten years.

Q It is a desirable thing is it not, to train men specifically in the Universities for this specialized variety of work?

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A Well, you are getting into the philosophy of education.

Q I do not want to get into anything like that.

A Frankly, it is my philosophy, my contention, that it is best to train men rather generally in principles and they will very soon learn to make specific application of their principles in practice.

Q If we have an expanding field here, then it would be probably advisable that we should give an opportunity or provide an opportunity to train our own young men in this particular avenue of endeavour is it not?

A Well, that seems to be the popular idea. I would not play up so heavily the particular specialized field for training. I would like to see it more general.

Q My reason was, for asking this, Dr. Brown, because according to the newspaper at least one of your statements was that we had to go down to get specialized experts from the United States in various fields. I am not questioning that. Obviously we have not got the men here who, from experience, or training, are exactly fitted for that work.

THE CHAIRMAN: I do not recall any such evidence.

MR. SHAW: I just read the newspaper report?

A I did not say anything of that kind.

Q MR. SHAW: Then the newspaper is quite wrong? Then we ought to have, if we can

do anything in that line, it might be valuable might it not? I simply read that statement from the newspaper report and perhaps I misread it. Perhaps it is quite wrong.

MR. PLOTKINS: The statement in the newspaper, as I recall it, said, or reported Dr. Brown to have said that there was an increased cost in refining because of the fact that the experts, the technical experts that were necessary to engineer the refineries and run them had to be secured elsewhere?

A No.

Q THE CHAIRMAN: That here we had to keep, perhaps, some more expensive and a greater number of technical staff or something to that effect. That was all, Mr. Plotkins.

A My statement was that primarily with the inability to get special services for electrical instruments and other control devices in Calgary and Alberta, as compared with a large industrial centre such as Chicago, for that reason the refineries operating in this territory had to keep on their staff men of that special knowledge and experience which the refiner in Chicago would not have to keep on his staff.

Q MR. PLOTKINS: That would not materially increase the cost of refining, Dr.Brown??

A It is one of the factors that would have an effect, yes.

Q Now I want to explore with you, Dr. Brown, the question of the basis - and I have no dispute with

all you have said to the Chairman about how you would proceed and go ahead and figure out the price for Turner Valley, except the original starting basis that you have set, and that is Montana.

A You mean that I have based everything on Montana?

Q As the main factor insofar as Regina and Calgary is concerned?

A Well, because it is the closest.

Q It is the closest, yes. I am going to explore that?

A That is not the sole factor though.

Q Yes, I understand so?

A All right.

Q If Turner Valley crude were to suddenly fail or completely disappear and we had to secure our 17,000 barrels daily that we require for the Prairie Provinces elsewhere, could we get that in Cutbank field at the present time?

A I doubt it.

Q You doubt it? So that we could only take what would be obtainable in Montana, as in the Cutbank field, at the price that it would be available. In other words if there were 5000 available at $1.10 or at any other price, that our going into that market might create, we would have to look elsewhere for 12,000 barrels then?

A Or the finished products comparable to that amount of crude.

Q True? But we have two refineries here, or several refineries, and they are not going to close. We

will assume they are not going to close down?

A They might have to close down under those conditions.

Q If they could not get crude in Montana they would have to close down?

A I do not believe there is any chance of bringing Illinois crude into the Regina Refinery and refining it there as compared with refining Illinois crude at Sarnia and shipping the finished products in.

Q Why not, Doctor? Crude can be brought in cheaper?

A Because of the freight rates. I have not made a thorough study of that, but I believe that the Illinois crude would be refined in Sarnia and shipped in as finished products rather than to bring the Illinois crude up into Regina and ship the finished products East. Whether that is true or not I do not know, but that is my present opinion.

Q That is contrary to experience where crude is always the cheaper product. That is it costs us less to transport it than the refined products?

A Sometimes, and sometimes not.

THE CHAIRMAN: Mr. Plotkins, I do not think you were here, but the witness, Dr, Brown, has made it clear that he has not really explored the situation in Southern Alberta in connection with Montana crude. He wanted time to do that and he did not want to go into it at this time because he thought he was not sufficiently informed. If you can keep that in mind, the Doctor will be back. I am correctly putting forward what you did say, am I not, Doctor?

A Yes.

Dr. G. G. Brown.

THE CHAIRMAN: If you could more or less leave that until he has gone into it then his answers will be based upon his examination of the situation and your cross-examination will then be of more value to us. Because right now he does not pretend to know about it.

MR. PLOTKINS: I am only dealing generally with the Prairie Provinces and the refineries in the Prairie Provinces, seeking to import crude and refine it into the manufactured products. Now, before the Sunburst field was discovered, or before the Cutbank field was discovered, we imported crude, at least the Imperial did, from Wyoming. Now is it not conceivable that if there were no crude in Turner Valley and you could secure approximately 5000 barrels in Cutbank - and I am using that 5000 barrels figure advisedly because it may be possible to cost more a barrel to produce and make available for this Western Canadian market 5000 barrels over and above what they now produce. Now it would be reasonable to assume they could go to Wyoming and get 12,000 barrels of crude to make up the difference?

A That is a possibility. I have not investigated that.

Q If we assume for a minute that they do go down to Wyoming and get the difference of 12,000 barrels, the price that they would have to pay in Wyoming could be ascertained. It would be the posted field price for a certain gravity crude?

A You mean it could be ascertained when as and if that

crude was available?

Q Yes?

A Yes.

Q Would it not follow that the crude from Wyoming laid down in Calgary or laid down in Regina would be more expensive, would cost more per barrel, quality being considered, than the Cutbank crude?

A I do not know.

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Q But the further the crude is away from the refinery the chances are that it will cost more laid down?

A If it costs the same at the well, yes.

Q Is it not rather striking that the different posted field prices as between fields are somewhat on a par taking aside local considerations?

A Under normal conditions in the average that is true.

Q So that if that is true and you go a longer distance to get the balance of your crude, you will have a higher laid down cost for that portion?

A Yes, everything else being equal.

Q Everything else being equal. Now, if we want to then average the cost of the 5000 from Cutbank and the 12,000 from Wyoming, we will add all the barrels together and all the money together we have paid out to strike the average cost?

A That is right.

Q Now if that situation that I have just painted were true, then you would arrive at a different posted field price for Turner Valley crude. Leaving aside all marketing considerations and territory for the time being?

A If I understand your question, you mean that if we had to develop 5000 barrels more in Northern Montana down here that in order to develop that crude we would probably have to raise the posted price.

Q No, I am not even asking you to go that far. I am going to ask you to accept it is possible to get 5000 barrels more in Nothern Montana and not even increase the price?

A You mean accept that as a fact.

Q Well, assuming that?

A You are going to assume that.

Q I am going to assume it because in the first place you have assumed you could get enough crude in Montana to supply these two refineries and your whole basis of computation is on an assumption?

A No, Sir, you are mistaken. I did not assume that we could get 5000 barrels more out of Cutbank at $1.10. I think I specifically stated I thought it was very unlikely.

Q Well then why should you take Cutbank posted field price as the point of departure for arriving at the value of crude oil in Turner Valley?

A Because there will be some crude available in Cutbank at $1.10, is that right?

Q Yes.

A Some. How much I do not know. All right, if there is some crude available in Cutbank field at $1.10 then that crude which is available at $1.10 is in competition with Turner Valley on an equal basis with Turner Valley as $1.30 at the well for 48 gravity and when both these crudes are to be refined in the Imperial Refinery at Regina.

Q I am asking you to assume that there is no crude available at the present time in Turner Valley sufficient to take care of all our requirements. In other words, there is only one well.

A All right, there is no crude in Turner Valley now.

Q Yes. You want to determine what you can afford to

pay for crude in Turner Valley if and when it is developed. You want to find the relative value of the Turner Valley crude with some other crude.

A Mr. Plotkins that is a situation that is impossible to analyse. You have to give me some conditions on which a man could work. If there is no crude in Turner Valley will I know what quality that crude would be if it were there?

Q Oh no.

A Well, where are we?

Q We have the Turner Valley Royalties well. We know there was crude in Turner Valley. We knew the character of that crude and the Imperial at that time determined to find what that crude was worth. Now, the chairman has asked you to give him your opinion as to how you would go about to fix or to find what is the proper price for crude in Turner Valley?

A Yes.

Q You have given as a basis the price of Cutbank?

A No, wait a minute. The very first thing I said was, I must first of all determine that territory that this Turner Valley crude is to supply. Then having determined that territory I then put the Turner Valley crude in competitive equilibrium in all of that territory with the crude and the refined products that might come into that territory from without. Now, if there is only one well in Turner Valley certainly the territory to be supplied by that well does not cover the large territory which is now being supplied by the Turner

Valley crude. And the very first thing you must give me is the quantity of crude that is available and the territory that is to be supplied by that crude.

Q Then we will go on your basis. We will take the actual fact. We have a field in Turner Valley and we have a market as ascertained of 17,000 barrels a day average for the present market. Now the Board is endeavoring to find out what is the fair price under these circumstances and they have asked you and you have said, well, taking into consideration the economic territory and taking into consideration the competition from the States, other crudes in other words, the economic territory is on a marketing basis and crude is on a crude basis, from Montana or elsewhere, you have said well, Montana crude could be purchased for so much and therefore we will compare Montana crude with Turner Valley crude and we will arrive at an economic fair price?

A For one particular operation only.

Q For one particular operation only?

A And that operation was the Imperial operation at Regina.

Q Yes? Well, we are dealing with the particular operation and we will take the Regina and Imperial refinery. Now the Imperial refinery at Regina if it sought to displace or to buy crude in Montana or elsewhere to replace Turner Valley, we will assume that tomorrow the Standard Oil of California for some reason or another acquired all the crude and it was a question of competing with the Standard Oil of California and the Imperial had to go out and

find crude to compete with it? That would be approximately the same situation. Now, if Regina goes into Montana to buy the crude would it be able to buy crude at the present time to take care of its requirements?

A All of its requirements?

Q All of its requirements in the Cutbank field. If the Calgary refinery did likewise, because we must take the whole territory.

A Wait a minute. I have lost you. I thought we were at Regina.

Q Yes?

A If the Regina refinery cannot get any Turner Valley crude, is that right?

Q Yes.

A That is your question? Could the Regina refinery go into the Cutbank and buy how much crude?

Q Buy its requirements.

A Which is about what, 4000?

Q 4000 barrels.

A Say 4000 barrels a day. I doubt if they could get it right now.

Q And it would be still further complicated if the Regina refinery of the Imperial went into the market?

MR. FRAWLEY: You mean Calgary?

Q MR. PLOTKINS: Calgary?

A Oh yes.

Q So if they had to find that 12,000 or whatever it is today they would have to buy in Cutbank only what was available and look elsewhere for the balance?

A Yes. Or they might ship in the finished products from Sarnia.

Q We will forget about the finished products. We will treat the marketing on the one hand and we will deal with the crude.

A As I told you earlier, we cannot forget about the competition between the different crude fields through the finished products. That competition is just as real as in the crude itself.

Q Well, I realize that Dr. but we will treat one at a time. When we are through with the crude we will weigh the finished product factors against it?

A All right.

Q Because naturally I quite realize the crude itself is not the whole thing. Them two refineries must go elsewhere to get the balance of that production?

A Than Turner Valley.

Q No, than Cutbank.

A All right, than Cutbank.

Q They will have to seek crude at the closest point and in this particular case, as I see it, it is Wyoming. And they will have to go and buy or secure the balance of their supplies if they are available there from Wyoming at the posted field price. In other words, Cutbamk crude is only one of the factors because it cannot supply all of the requirements. Therefore, you should take into consideration more than the Cutbank price of crude. If you are going to be on a fair basis and a fair commercial basis you will be on the same basis as the marketer that sees a competitor sells

[illegible]

gasoline for ten cents when he is selling his for fourteen cents but after investigating he finds that marketer is only in a position to supply 1% of his market so therefore, he is not going to cut the price on his 99% in order to meet the 1% marketer. That is the position the crude purchaser is in, or the crude seller?

A Are you asking me a question?

Q Well I am coming back to that question. If Cutbank could not supply the total requirements, is not it obvious that other considerations must be taken into this primary basis of arriving at a fiar price for Turner Valley crude?

A I have repeatedly stated other considerations should be made, such as competition between the finished products in Southern Alberta and from Illinois. But if I understand your position, if I can be of help to you, you are trying to take the stand that the price for Cutbank crude that would be necessary to develop the 5000 barrels of additional Cutbank crude in order to supply the Regina refinery is a price which should be considered to make Turner Valley in competitive balance with Cutbank. Is that your position?

Q Not quite, but it is to this extent that I am assuming even that there will be no rise in the price of crude in Cutbank but it will be necessary to go elsewhere for the balance of it. Therefore, your average cost of crude that you will require will be considerably more than $1.10 and that average cost is what you should take for the basis of arriving at a fair price of Turner Valley crude.

A Well I disagree with you entirely.

A Well I disagree with you entirely because your very discussion was based on an assumption which you gave us which was that there was no Turner Valley crude available and study which is based upon assumptions or conditions which are contrary to facts will be absolutely valueless. The only possible study which can be of any help is a study based on conditions as they actually exist or upon estimates which are as near to the truth as we can possibly make them and if we are to assume there is no Turner Valley crude here and then try to figure what the price of Turner Valley crude would be if there were none, of course that price is of no help to this Commission in determining whether or not the present price is a fair one. We must face the situation as it is and that is, there is a certain amount of Turner Valley crude being marketed and seeking a market and so long as that Turner Valley gets that market then it must be in competitive balance when it is supplying that market with the other crude that begins to displace it. There is no use in trying to put one barrel of Turner Valley crude a day in a competitive balance under the present conditions and so that is the basis which would determine the prices for Truner Valley crude because there is more than one barrel of Turner Valley crude available on the market. Supposing there were 100 thousand barrels of Turner Valley crude actually reaching the market, the price would then be still different and any price which you might set based upon an assumption that there is no Turner Valley crude is absolutely of no value. The fair price for Turner Valley crude must depend upon the amount of Turner Valley crude

which is reaching the market.

Q Yes, but Doctor at the last we did, I did ask you to take the actual facts, that there were 17,000 barrels of Turner Valley crude available for this market and what we want to find out is what is its value in relation to competition and so there is no question now of taking or assuming----

A Then you would never buy more than about 10 barrels down at Cutbank because if you are going to still allow the Turner Valley crude to supply Regina you cannot take very much Cutbank crude.

Q Well we are not taking any and all I want to find out is what is its value in relation to Cutbank crude or any other source of supply?

A Yes, and I have set forth the basis upon which I believe that should be computed and it shows that with Cutbank crude at $1.10, Turner Valley crude of 48 gravity should have a price of $1.29½ in the field at Turner Valley based upon Imperial's operations at Regina.

Q THE CHAIRMAN: And if I may interject, if that were the premise, Cutbank crude at $1.10, would we not have to know what made Cutbank crude $1.10 instead of $1.00 or $1.20?

A Well----

Q To be really consistent, feel that we were safe in making an answer?

A Well if the Imperial can go into the Cutbank field and buy 500 barrels per day of crude at $1.10, then it is a toss-up whether they do that or run Turner Valley crude.

Q MAJOR LIPSETT: Dr. Brown, taking it that 17,000 barrels a day are required and that in the first in-

stance there may be 5,000 barrels of that available in Cutbank and no more, now to what extent or in what way could Cutbank then affect the price of Turner Valley crude so far as the other 12,000 barrels are concerned, which Cutbank cannot supply?

A Well I am assuming that there is going to be one price in Turner Valley and that price is the lowest price. I do not believe it is humanly possible to go into that field and maintain conditions in a satisfactory state paying some producers $1.50, another $1.30 and somebody else $1.20. I think we have to have a uniform price in the field.

Q Then on that assumption it is quite clear that Cutbank cannot supply the whole market, would Turner Valley then be in a position to say "Well we will not supply you with any unless you take your 17,000 barrels from us at our price of cost plus a reasonable profit".

A Well let me see if I can analyse that situation; in other words the Turner Valley producers all get together and say they want $1.50 for their crude?

Q Yes, assuming $1.50 is cost plus a reasonable profit?

A Well that doesn't enter into the calculation; it is just that the producers have all gotten together and decided they would not sell any crude unless they got $1.50.

Q They will not supply Imperial at all unless they take all their requirements from them?

A All of the 17,000 barrels.

Q Yes?

A And I am an employee of the Imperial trying to find out what to do.

Q Yes?

A Has the Imperial to take 17,000 barrels a day?

Q Well that is the market if the Imperial was taking it all?

A Well I would have to study that a little more carefully because it would mean that the Imperial would either have to bring in other crude here and see how it would balance out or consider other crudes at Regina and I would go at it exactly the same way as I went at the other problem. I would, instead of determining what the price should be of Turner Valley, I would go backwards over the same road and say the price at Turner Valley is $1.50 and then figure out what it would cost to bring other crude in in the average at Regina and Calgary and see whether or not the over-all operation would be more economical to bring in the other crude and run it at whatever price could be obtained or take the whole thing from Turner Valley.

Q Well that would mean then that, would it not, that, assuming that Turner Valley then could compete with Illinois or the other crudes that they would consider, that Cutbank would cease to be a factor altogether or would it?

A No, you mean under those conditions.

Q Yes?

A Oh, Cutbank would be a very important factor under those conditions.

Q The supposition which I was putting, Dr. Brown, is that Cutbank cannot supply the whole market but they can supply 5,000?

A They can supply 5,000.

Q Yes?

A That amounts to about one-third of the whole requirements.

Q And Turner Valley says "We will supply you only on the basis of your taking the whole requirement from us"?

A No, I think Cutbank would then become even a more important factor than it is now.

Q Well would not the comparison then be, we have that 5,000 from Cutbank plus the 12,000, which might be $2.00 from elsewhere?

A Well if it were $2.00?

Q Whatever it is?

A I would have to get those figures and see where it came out and that is exactly what it was.

Q And could not Turner Valley then retain 17,000 of the market as long as they were at a price less than the price of the 5,000 from Cutbank and 12,000 from elsewhere?

A Oh under those conditions, but that is not a competitive condition.

Q Well, but what I am trying to get at is there any real competitive condition?

A Yes, the very fact that that condition which you have outlined does not exist is evidence that there is a really competitive situation; the very fact that the $1.30 at Turner Valley is the price which has been arrived at and the very fact that the Regina refinery is operating and supplying the territory that it is supplying on Turner Valley crude when the Turner Valley crude is $1.30 and that the Cutbank crude is not available in any appreciable amount under $1.10, is to my mind very clear evidence that that competitive condition exists. If on the other hand the Turner Valley price were $1.50 and the Regina operation was being conducted on Turner Valley crude and the posted price at Cutbank

were $1.10, then I would say we did not have competition. We then have some kind of monopoly or desire on the part of the Imperial to market their own crude from Turner Valley regardless and they believe they can continue marketing their own Turner Valley crude and get perhaps a specially high price for their product.

Q Then on what ground, Dr. Brown, do you come to or get the assumption or come to the conclusion, if you have done so, that there is any real competition in the fixing of the Turner Valley price?

A Well might I continue, that is really the same thing I was trying to say, if the Imperial had,-this is contrary to facts,-but if they had found it possible to pay $1.50 for Turner Valley crude and market their products over the same territory that they are now doing, it would indicate that then the Imperial must have had some kind of monopoly in through the Regina territory and possibly Southern Alberta or in Northern Alberta or some other place, so that they could get a non-competitive high price for their finished products because they are paying a non-competitive high price for the raw material, crude oil and no refinery can exist for any length of time paying a non-competitive high price for the crude oil unless they correspondingly receive a non-competitive high price for the finished product and the very fact that the Turner Valley crude oil is now receiving a price which to the best of my calculations is not competitively balanced with the finished product from the other crude fields and also with the crude oil itself from the Cutbank field when laid down at Regina, to my mind is evidence that the Imperial Oil Company is getting a com-

petitive price for its finished product.

Q Well now what do you exactly mean by a competitive price for its finished product; if you eliminate all the major companies operating here, what competition is there in say Northern Alberta?

A Well now I did not say they were actually in competition. What I said was that they were getting a competitive price, in other words they may still have a monopoly but they have so set the prices and those prices are what would have been arrived at under competition. There is such a thing as a competitive price for crude oil and a competitive price for finished products, whether or not that price is actually arrived at by competition, by regulation or by the fixing of rates, it does not make any difference, there is still that competitive price which can be computed. Now one way of getting at a competitive price and seeing that it is maintained would be regulation; another way is by free competition; another way might be by just good judgment on the part of the company to maintain the competitive price even if they had a monopoly.

Q And you use the word "competitive price" as not necessarily a price fixed by competition?

A No, but the price which would be fixed by competition whether or not the competition exists.

Q MR. PLOTKINS: Dr. Brown, is the Mid-Continent market for petroleum markets known as Group 3, the basic market for refined products?

A Well it was at one time.

Q It was?

A I would not say it is now; over so much territory as it used

to be anyway.

Q But it still is the primary market?

A No I do not think so; it is the major basis for setting prices in the two Southern States, South of the Great Lakes perhaps, but it does not set the price of the Great Lakes territory or Ohio.

Q It doesn't?

A No.

Q A distributor in Manitoba, wanting to purchase gasoline for instance, he would want to get the best price available in the United States, I mean if he was going to compete with the Imperial Oil products from Sarnia, as sold by the Imperial Oil, he would want to get the best price, he would want to purchase his products at the lowest possible price, would that not be right, as a marketer?

A Well I guess so, I do not quite understand your proposition yet.

Q Well what I am getting at is in order to successfully compete with the Imperial Oil marketing department, the distributor would seek to buy on as good a basis as possible and it is not a fact that the imports, that the importations that he would be able to make from the United States would be sold to him on a group 3 basis?

A I do not know.

Q Going into Manitoba?

A I do not know.

Q That is my experience?

A Well I do not know.

Q That we do buy, in fact all of our prices that the Imperial Oil sets in this Western country, is based on

Group 3 competition?

A No I do not think so.

Q Wherever it can reach. Now I am not saying all over, but we will take in Manitoba, what determines the refined oil market, and perhaps you can tell us that?

A I have made no study of that at all, and I am not prepared to discuss that.

Q Then I am going to ask you another thing, is there any place in the United States where the refined oil price or the refined oil market has any direct relation to crude?

A You will have to amplify your statement, I do not quite understand you.

Q Is there any basic market in the United States that relates selling price to the cost of crude oil or the cost of crude oil to the selling price of gasoline?

A Is there any basic market.

Q Yes?

A Well over a period of time that relationship of course exists and if the price of products goes up the price of crude usually goes up with it and vice versa but I do not know of any particular market. I do not follow you frankly.

Q Well Group 3 in the trade is understood and it is accepted as the basic market for the price of petroleum products in the United States?

A I disagree with you.

Q It may vary at times and Texas may temporarily affect it but all the quotations we have in the trade magazines certainly indicate that Group 3 is the dominating factor, to simplify it, Dr. Brown, I might ask you to agree or disagree,, in the Mid-Continent, group 3 prices, we have the

[illegible]

lowest prices for gasoline for a given quality in the United States, is that correct?

A I think in general that is probably true.

Q That is true?

THE CHAIRMAN: What was that statement again.

MR. PLOTKINS: I said----

THE CHAIRMAN: The witness said something was probably true and I didn't catch what it was.

Q MR. PLOTKINS: I said that in Group 3 in the Mid-Continent market, the gasoline market, we have the lowest price per gallon that is actually a fact in the United States and the Doctor agrees?

A I said that is probably true.

Q Probably true?

A I do not know for sure but I think it is probably true but so far as your Group 3 goes, I find a couple of pages of quotations here and I find a column over to the right giving Group 3.

Q Yes?

A So I cannot agree with you that Group 3 is the basic structure for the United States at all. Now I am not here discussing markets.

Q No?

A I specifically kept away from it and what I am trying to do is trying to be of help to you and I think I could be of more help,if you are worrying about the price of crude or refinery operation, if you would come out flat-footed and say what is in your mind and say what you are trying to get at, I could answer your question directly but if you work at it through all these marketing structures and things

of that kind, it is going to be very confusing and I am afraid that I cannot be of very much help to you.

Q Doctor, there is some place in the United States where there is a direct relation between the price of crude and the price of gasoline?

A I think that is true all over the United States in general.

Q Yes, but in other parts than the Mid-Continent, there are other factors, local factors, which influence the price of gasoline?

A No more than there are in the Mid-Contient.

Q Well I cannot see how I can question you or cross-examine you, doctor, without referring to markets because after all crude is valueless unless you turn it into products and sell them?

A Well perhaps you had better wait until all the evidence is in on markets and crude and you will have the whole picture.

Q Perhaps, but you will notice if you look at these markets that not only the Mid-Continent and the Michigan and the East and West refineries quote their prices basis Group 3?

A No, that is not true. I know the price in Michigan is not set basis of Group 3. You are right now in my home country when you talk about that and I happen to know something about that.

Q You mean the local tank waggon is not set?

A That is right.

Q But the tank - car market?

A There is nothing sold on the tank car market out there.

Q There is nothing?

A No, it is the same situation as exists here.

THE CHAIRMAN: I suppose everyone other than

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

the members of the Commission know, but what do you mean by "Group 3"?

MR. PLOTKINS: Group 3 is Oklahoma and Kansas, that particular producing territory which was the dominant producing territory for a good many years and which has established----

THE CHAIRMAN: Oklahoma?

MR. PLOTKINS: Oklahoma and Kansas roughly.

THE CHAIRMAN: Those two were called "Group 3"?

MR. PLOTKINS: No, that is known as the Mid-Continent and then the railways established a set of rates for the different parts of the United States and that set of rates did not vary even if one refinery was in one part of the States and another refinery was 400 miles away, they still take the same rate to the given point of export, so that that territory in which the railways published rates, which were competitive to some points, became known as "Group 3 basis" and today that is still a factor, that while the price itself is not governed by Group 3, the refiners in making the prices to the purchasers use that factor of freight to destination to balance their price as against the group 3 so that they are then in a competitive position with the Group 3 refiner. Now that is what I am trying to get at.

Q THE CHAIRMAN: "3" came from what, do you know?

A It was a group of or rather a railway rate, and what he has reference to is that the Group 3 freight rates which are freight rates from anywhere in this territory to any one of

these Cities.

Q THE CHAIRMAN: Oh I see, it is just, that "group 3" is a designation probably given by the railways themselves?

MR. PLOTKINS: That is right.

WITNESS: For a group anywhere in that group, it is a group of cities and territories, I do not know the exact boundaries of it.

MR. FRAWLEY: A group of shipping points.

WITNESS: Yes, it is a group of points and anywhere from anywhere in that group of points the freight rate would be the same.

Q THE CHAIRMAN: I would suppose from what I have seen, that the railways speak of it as "group 3" in connection with their freight tariffs?

A That is right.

Q Just the way they might call it "schedule C"?

A That is exactly right.

Q They call it "group 3"?

A That is right or "group 3 freight rate".

THE CHAIRMAN: I am sorry to interrupt you.

Q MR. PLOTKINS: Well the United States is divided up for freight purposes, that is for oil purposes, it is divided up into groups from one to six as I remember it?

A I am not sure about those details.

Q So that you say in the main, in the Mid-Continent, the group 3 territory, the originating territory, group 3, that the price for gasoline is the lowest of any part in the United States, on an average?

A I think that is probably true, I am, just a moment, here is the latest quotation I think, Oklahoma 70-72 octane is 5 to 5¼ on June 5th; West Texas the same, is 5 to 5½; Central West Texas 5-1/8; East Texas, that is not listed, and so on, so it is about as low but it is not always the lowest.

Q Temporarily it may not be, temporarily there are variations?

A Yes, but on an average it is about as low as any.

(Go to number 9270)

Dr. G. G. Brown.

Q So that there at least the margin between the sale price of gasoline and the posted field price of crude is at the lowest?

A Oh, possibly, I do not know.

Q Well, in the Mid-Continent we have a posted field price of $1.10 for a certain gravity?

A Is that a question?

Q Yes, I mean the posted field prices of particular gravities in Mid-Continent are substantially even?

A The Mid-Continent ranged from 70 cents to as high as $1.10. $1.10 is the highest and the lowest is 58 cents, that is posted here.

Q That is for very low gravities?

A 58 cents is for 25 to 25.9 gravity and $1.10 is for 40 and above.

Q And that 40 and above at $1.10 on an average is the prevailing price throughout the average fields in the United States?

A Oh, I do not know.

Q With local variations?

A Most of the Mid-Continent pipe line crude is about 37 gravity perhaps?

MR. ~~KNODE~~: Campbell 36 to 36.9?

A Thank you. That is $1.02. So the average Mid-Continent would be $1.02.

Q MR. PLOTKINS: Would that be substantially the same as the same quality of oil in Texas for instance?

A Well East Texas is a little bit better oil in some ways. East Central Texas is listed at a few cents more for the same gravity. East Texas is $1.04 for

that same gravity. That is what it should be.

Q And in the Mid-Continent.....

A In the Panhandle it is 88 cents. That is in the Panhandle for the same gravity. Of course, it is much lower.

Q In the Mid-Continent field we have a comparatively large number of large purchasers posting a price, is that not correct?

A Well, in the Mid-Continent it lists the Standard Oil of Indiana, the Carter-Magnolia, the Sinclair, the Shell and Continental Texas Company, so there are at least four groups that post their own separate prices, and they are listed here.

Q So that there is competition between large purchasers for the crude available?

A Well probably. I think they work together pretty well on it, not to undercut each other too much.

Q THE CHAIRMAN: Just a minute. Why do you say that?

A Well, I doubt very much if anyone of these purchasers would go in and all of a sudden drop the price 30 cents or something like that. Once in a while it is noised around one is going to cut its price. But I mean they are trying to strike a balance. One of these purchasing groups may feel that the price is too high, and that there is too much drilling being done and so on, and they may decide "Well, we will have to cut the price." The other group will say "No, we are going to keep it," and over a time you will find that difference, but it won't stay that way very long. That is competition.

Dr. G. G. Brown.

But it would be rather chaos if four different purchasing groups continued to vary their prices at random. And they find it best to kind of work it on a uniform price, and post about the same price, and that is what it is here.

Q MR. PLOTKINS: It is the same price.

A Yes, for all four of them it is exactly the same. 33 gravity. Most all of the crude is above 33 gravity, so to all intents and purposes the prices posted by these four purchasing groups are the same. The prices differ only in the low gravity crudes and there is very little of that crude sold.

THE CHAIRMAN: If it is to be accepted by men like yourself that the price is arrived at as a result of a conference, and one need not look for impropriety or criminality,- but they put their heads together and say what the price should be?

A Yes.

Q That is what you would expect in a case such as we are talking about?

A They do it in an orderly manner instead of a chaotic manner. There is competition there. It is a price arrived at on the basis of free competition.

Q That is what I am wondering about. I see with good sense, the heads of the four groups we have been mentioning might meet and say what is the fair field price, or what is the price we four shall fix, whether it is fair or not. It is

Dr. G. G. Brown.

fair to them would be the principle consideration, generally is in the business world. Is that free competition as you would define it or is that just a matter......

A It is not done in that way. There is many times disagreement between these groups. You will find price changes but not for a long period or for any appreciable period do you find a different price. In other words, if one of these groups thinks the price is too high they go in and cut the price. Perhaps he is wrong, and if he is wrong it is only a few weeks before he is back up again to where he was before. Perhaps he is right, and if he is ~~right then the~~ others come down and meet it. Therefore, it is an orderly setting of the price. Because they are all tied up with gathering systems, and if one group is always below the others that group is going to lose its connections because the producers do not want to sell their oil to the lowest competitor all the time.

Q And you say, and of course one follows, there need not be cut-throat competition to be real competition?

A It is orderly competition.

Q And the question is where is that line between competition which is not cut-throat and an arrangement whereby there is no competition at all?

A That is kind of hard to draw sometimes, perhaps.

Q Yes, I think so.

Q MR. PLOTKINS: In the Mid-Continent with four large companies posting a price, and on an average striking the proper price, as you say there

[illegible]

talk to them would [illegible] consistently, [illegible] is in the business world. Is that free competition as you would define it or is it [illegible] a matter.....

[illegible] way. [illegible] groups. [illegible] will [illegible] changes [illegible] any [illegible] period do you find a different price. In other [illegible] these groups [illegible] price is too high they go in and cut [illegible] price. Perhaps he is wrong, and if he is wrong it is only a few weeks before [illegible] to whom he [illegible]. Perhaps he is right, [illegible] is right [illegible] the others come down and meet it. Therefore, [illegible] setting of the prices. [illegible] they [illegible] tied up with gathering systems, and if one group is always below the others that [illegible] is going to lose its connections because the producers [illegible] want to [illegible] their oil to the lowest competitor all the time.

And you say, and of course one follows, there need not be cut-throat competition to be real competition?

It is certainly competition.

And the question [illegible] is that line between competition which is not cut-throat and an arrangement whereby there is no competition at all?

That is what we have to draw sometimes, [illegible].

Yes, I think so.

[illegible] In the Mid-Continent [illegible]

[illegible] changes in posting a price. [illegible] striking [illegible] price, as you [illegible] there

is, if one purchaser is too low he might not be able to enforce his price and therefore the average price will be maintained. That is the fair average price for the four instead of but one will be maintained. Now is it not a fact then that at that point at least there is also competition in the sale of refined products?

A I think there is, without doubt.

Q Certainly. So that we find then in that group refined products moving to the United States markets in competition with refined products from other fields, and these particular sellers of these refined products from the Mid-Continent can only go as low as the crude will let them in the price. In other words, they are on a business basis and they must ~~take into consideration~~ what they have paid for the crude plus the cost of refining or plus a profit.

A If any.

Q If any, yes. If conditions will permit. On the average they do make a profit?

A Not in the last few years. On the average the Mid-Continent refiner has been in bad shape.

Q Are you talking about the independent or the major companies?

A Well, what did you have in mind?

Q I am talking of the industry as a whole.

A Yes, I say the industry as a whole in the Mid-Continent has been in very bad shape for some time.

Q You say there is a direct relationship at least in the Mid-Continent between the sale price of the gasoline and the posted field price that they pay

for crude?

A What I said earlier was in the aggregate over a reasonable period of time, and over the whole area there was a very definite relationship between the price of the finished products and the price of crude.

Q Yes. That is right. That is the conclusion I wanted you to come at.

A I stated that quite a while ago.

Q That is all right. I wanted to bring out these different points for the benefit of the Commission.

A All right.

(Go to Page 9276-)

Q Why then in Alberta here should not we take the same basis in arriving at our crude values in Turner Valley?

A I think you should. That is what I have done.

Q No, you have, at least my impression is, that you have taken mainly the price of Cutbank crude and translated it into the price for Turner Valley crude?

A The same thing is done here, absolutely. The price of Michigan crude versus the price of Illinois crude versus the price of Mid-Continet crude versus the price of East Texas crude laid down at all the different points. That is exactly what has happened here.

Q The price of crude in Montana may be affected by a number of considerations that would not apply here?

A By a number of considerations you mean a number of specific instances?

Q Yes, specific local conditions.

A Yes, conditions at Calgary may be different than they are down in Montana, that is right.

Q No, I mean that the price of $1.10, in fact you considered yourself, and made the remark you felt it was pretty low, that price of $1.10 in Cutbank.

A Well, I said I doubted if the Imperial Oil could go into the Cutbank field and buy an adequate amount of crude to keep their refinery running at $1.10.

Q I understood you also in general to make the remark that the price of Cutbank was reasonably low?

A Now I think that I said that $1.10 is considered to be a reasonably low figure for evaluating the competitive balance of Turner Valley. I did not say $1.10 was the reasonably price for the crude. I said the figure of

$1.10 was a reasonably low figure for that purpose because I doubted if the Imperial Oil Company could get a daily delivery of 2000 barrels of crude at $1.10.

THE CHAIRMAN: Mr. Plotkins, we will be rising in a few minutes. If there is anything particular you want to ask as distinguished from that, you might ask it now.

MR. PLOTKINS: I was going to go on to the matter of the skimming plant but I think it would be better for the Dr. to study the statements we have prepared and that we will present before I examine him on that phase. So that it would be better to wait.

THE CHAIRMAN: All right.

MR. COMMISSIONER LIPSETT: Dr., there is one point I would like you to give some consideration to on the real relationship of the price of crude to the refinery price. We find, as I gather, that for the Southern Alberta Turner Valley crude cannot be used at more than 92 cents on the one hand?

A Pardon me.

Q That Turner Valley crude cannot economically compete in Southern Alberta at more than 92 cents?

A I am not aware of that. I have not made any such calculation myself.

Q It has come before us and perhaps you would consider it. It was on that basis apparently that the price of $1.30 was averaged out?

A Somebody might have had that idea of it. That I do

not know.

Q Notwithstanding that we find there is a great deal of Calgary gasoline going down to that part of the province. On the other hand, we have a figure that for the Calgary refinery, the Calgary area, the Turner Valley crude price could be $1.52.

A Oh, I get what you mean.

Q Yet we find although it is only $1.30 that notwithstanding that there is still a considerable quantity of refined products refined from Montana crude coming up and being marketed in this very area. It seems to me there are some other factors rather than that economic price of crude that enter into it and perhaps you would give some consideration to that and give us whatever information and views you have about it when you do come back.

THE CHAIRMAN: All right. We will adjourn.

(At this stage the hearing was adjourned until 10.30 A. M. June 19th, 1939)

The Province of Alberta

IN THE MATTER OF THE PUBLIC INQUIRIES ACT

—and—

IN THE MATTER OF a Commission, dated the 12th day of October, A.D. 1938, to inquire into matters connected with Petroleum and Petroleum Products

Commissioners:

The Honourable MR. JUSTICE McGILLIVRAY (*Chairman*)

—and—

L. R. LIPSETT, ESQ.

Session:

CALGARY, Alberta JUNE 19th, 1939

VOLUME 81

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WITNESS:

. . . .

EXHIBITS

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[illegible] [illegible]

[illegible]

[illegible] . . . . [illegible]

[illegible]

[illegible] — [illegible]

[illegible] — [illegible]

[illegible] — [illegible]

[illegible]

[illegible]

ALFRED ELMER HALVERSON, having been first duly sworn, examined by Mr. Frawley, said:

Q Mr. Halverson, you are the director in charge of marketing of Imperial Oil Limited?

A No, I am a director with jurisdiction over western marketing.

Q You are a director of the Imperial Oil and have jurisdiction of the marketing of all of the products of Imperial Oil Limited in Western Canada?

A Yes.

Q And one of the marketing divisions of your company is the Province of Alberta?

A Yes.

Q And you have come here today to present the statements of your company to this Commission in the matter of marketing petroleum products?

A Yes.

MR. FRAWLEY: Mr. Nolan.

TO MR. NOLAN:

Q There is in the hands of the reporter and copies available for the Commissioners, the first part of the presentation of Mr. Halverson, and I think I ought to explain to the Commissioners that it falls into four parts, and there are four different volumes dealing each with a separate part. The first one which the Witness proposes to deal with is the General Review of Marketing Operations in Alberta; the second is the Price Structure in Alberta; the first is the General Review of Marketing Operations

in Alberta, and secondly the Discussion of the Price Structure in Alberta; thirdly, Jobbers' Prices and Sales in Alberta, and fourthly, Lubricating Oils with a special reference to the sales, distribution and prices of lubricating oils.

MR. FRAWLEY: We might mark them all now.

MR. NOLAN: There might be something get in between, and with the permission of the Commissioners, we would ask to have marked now the first of these presentations entitled "General Review of our Marketing Operations in Alberta".

(DOCUMENT PRODUCED HERE MARKED AS EXHIBIT "314"

MR. FRAWLEY: Of course, Mr. Nolan suggests the only objection to making them all Exhibits now is that something might intervene. On the contrary, I think if we had all of these together, we would know that they are Mr. Halverson's statements and later they might be available.

THE CHAIRMAN: It is for Mr. Nolan to say. He is offering them.

MR. NOLAN: Knowing we would not finish by any manner of means this morning, we did not bring the fourth volume with us. However, that might be put in this afternoon, or if we might just have the first one marked this morning.

Q MR. NOLAN: Mr. Halverson, would you make a note on that copy of yours that it is Exhibit "314", because it might be necessary to refer to it from time to time by its Exhibit number.

A. E. Halverson

THE CHAIRMAN: If you like, Mr. Nolan, we can put in Exhibits "315" and "316" and we will reserve the number "317" for the other one to be put in later?

MR. NOLAN: Yes, we can do that.

Q MR. NOLAN: You have the second and third volumes?

A I have only the first and the second.

MR. NOLAN: I think it would be less complicated if we could do it only one at a time.

THE CHAIRMAN: All right.

Q MR. NOLAN: Now, Mr. Halverson, if you would be good enough to take Exhibit "314" entitled "General Review of Our Marketing Operations in Alberta" and present that in your own way to the Commissioners. The Commissioners have their copies.

THE CHAIRMAN: Thank you.

Q MR. NOLAN: All right, Mr. Halverson.

A The following data summarizes principal Physical Equipment and Personnel employed in our Direct Marketing tions in the Province of Alberta, as of December 31st, 1938:-

Office Buildings - Calgary and Edmonton	2
Main Stations	3
Number Bulk Agencies	267
Number of Warehouse Agencies	14
Number of Company-owned Service Stations (Land Owned)	62
Number of Company-owned Service Stations (Land Leased)	7
Number of Service Stations - Third Party Lease	8
Number of Company-owned Trucks	9

A. E. Halverson

Number of Steel Barrels	94,680
Management	3
Number of Office Staff	74
Number of Salesmen and Supervisors	17
Number of Auditors	4
Total Other Salaried Employees	49

We list on the following pages, sales of the principal products we marketed direct in Alberta in the year 1938.

Gasoline	21,357,501	gallons
Turner Valley Naphtha	1,503,011	"
Refined Oil	1,122,449	"
Distillate	1,225,408	"
Light Fuel Oil	1,309,627	"
Bunker Fuel Oil	8,977,234	"
Asphalt	2,489,670	"
Marvelube	634,562	"
Other Lubricating Oil	549,877	"
Grease	120,759	"
Number of Atlas Tires	12,324	
Number of Atlas Tubes	16,159	
Number of Atals Batteries	3,466	
Atlas Accessories	$35,729	

Practically all of our supplies of White Products in Alberta are shipped from the Calgary Refinery, either in tank cars or by truck. Generally speaking, we supply all points located more than 100 miles from the Calgary Refinery by Tank Car. Our Lubricating and Grease Requirements are principally supplied from our Refinery at Sarnia, Ontario, to Calgary and Edmonton, from which points same are re-distributed.

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Our total sales of Gasoline, Kerosene and Distillate - commonly known as White Products - for the year 1938 - were as follows, by months:

January	-	3.6%	July	-	9.9%
February	-	2.9%	August	-	10.4%
March	-	4.9%	September	-	13.7%
April	-	6.7%	October	-	13.2%
May	-	11.2%	November	-	8.0%
June	-	10.0%	December	-	5.5%

You will thus note that 68.4% of our total annual sales of White Products are made during the six months ending November. Exclusive of Calgary and Edmonton, the percentage is 70.5%.

Our distribution setup therefore in Alberta, must of necessity be such that we can take care of peak requirements, as it is urgent that during the threshing season there be no breakdown in supplies.

Our principal plants in Alberta are located at Calgary and Edmonton. A very large portion of all the Lubricating Oils, Grease, Tire and Battery requirements of Alberta are shipped from these two central points. This, of course, necessitates adequate warehouse facilities. At our rural agencies we usually have a 20x30 galvanized warehouse for the storage of barrel and package goods. Where sales volume and transportation savings warrant, we have generally installed, one or more 11½x20 storage tanks, capacity 13,000 gallons, on sites leased to us from the Railways at $10.00 per annum. The estimated cost of a 20x30 galvanized warehouse at the present time is approximately $650.00. The estimated cost of one

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$11\frac{1}{2}$x20 storage tank installed complete with pumps, pipes and fittings, et cetera, is approximately \$1,200.00. The estimated cost of a plant consisting of a 20x30 warehouse and two $11\frac{1}{2}$x20 storage tanks complete with tank car unloading rack, scales, pumps, pipes and fittings, et cetera, is approximately \$3,244.00.

With the exception of Calgary, Edmonton, Lethbridge, Wetaskiwin and Ponoka - which we operate on salary - all our agencies in Alberta in 1938 were operated on a commission basis. The agent receives the following commission rates:

White Products	2¢ per gallon commission on sales to consumers at posted tank wagon price. 1¢ per gallon commission on sales to dealers.
Lubricating Oils	3¢ per gallon commission on Mobiloils 4¢ per gallon commission on Polarine 5¢ per gallon commission on Marvelube

Those are the commission rates when sold to dealers and double these commission rates when sold to consumers at list prices.

Other Lubricating Products and Greases	5% off the net invoice price.

The commission agent is the sole agency in his town for the distribution of our products and sells on Imperial invoices at prices established from time to time by the Company. He is responsible for cash received, inventory on hand, unauthorized credits, abnormal stock losses, and all expenses in connection with the operation of the agency, except the rental of the site from the railway, taxes and maintenance of the plant. Where a commission agent operates motor equipment, he either buys

A. E. Halverson

same outright or we advance up to 50% of the value of the equipment, to be repaid in monthly installments within two years. Where we do not have bulk storage for a given product at a certain agency, supplies are delivered by truck from the Calgary Refinery or from the nearest commission agency at which we have bulk storage for such product. The supplying commission agent on such deliveries receives a commission of ½¢ per gallon, and a cartage allowance which is usually 1¢ per gallon, but sometimes higher depending upon distances. Such deliveries from one agency to another are commonly known as inter-station transfers. We are tabling as an Exhibit, copy of our standard Commission Agency Agreement.

We do not company-operate any of our service stations but lease them to tenants at a basic rental of 1¢ per gallon which varies with the type of service station and equipment provided. The tenant purchases his products from us at the same price as the dealer and is responsible for all operating expenses at the service station except taxes and maintenance, although in certain cases we have assumed part of the expense of lighting. He is free to hire his own men and to set his own retail price. We table herewith as an Exhibit, standard form of our lease arrangement with our service station tenants.

Exclusive of our company-owned service stations, we supply 700 dealers in Alberta who have underground tanks and gasoline pumps for retailing their products. In addition we supply 127 consumers by tank wagon. All other consumers, including 693 small dealers such as hardware stores, et cetera, buy their requirements of petroleum products in barrels or cases.

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We do not loan equipment such as pumps and tanks to dealers in Alberta, as is the practice generally in the United States. We sell pumps and underground tanks to the dealer for a cash payment, balance in equal monthly installments repayable in five years.

Steel barrels are loaned to farmers and others, with the exception of shipments into remote areas such as the Waterways, where the barrels are charged for at $8.00 each, returnable for credit at the same price if in good condition.

Some Oil Companies in Alberta operate only in selected areas, but we feel it is our responsibility to have our products available for prompt service in every town in Alberta in adequate quantities to meet peak demands. This not only includes Motor Fuels and Lubricants for farmers and dealers, but Aviation Products, Industrial Lubricants, Fuel Oil, et cetera, to supply promptly the needs of industrial organizations in Alberta, no matter where they may be located.

Alberta covers an area of 248,800 square miles, much of which is relatively sparsely settled, but nevertheless, entitled to dependable service at prices that do not discriminate against them as compared with more settled areas. On the other hand, the wise variations in seasonal demands adds to our difficulties in reducing marketing expenses, because a staff and plant must be kept intact 12 months of the year to take care of peak requirements even though our sales during the winter months are practically neglibible.

A. E. Halverson

Smaller companies operating principally within easy trucking radius of Calgary do not have the same problems. They can more their products by chartered trucks into dealers' underground storage and we assume can therefore very materially curtail their expenses during the period of low consumption. If during the period of peak consumption their service proves inadequate, no particular embarrassment results to the consumers of Alberta providing our Company with its facilities for widespread distribution is in a position to give uninterupted deliveries. An adequate dependable source of quality products of every kind for every need always available winter or summer at all points in Alberta, is essential from the standpoint of the uninterrupted operation of Alberta's farms and factories and when comparing our operations with those of local companies catering only to selected areas this should be taken into consideration.

For 12 months ending December 31, 1938, our total marketing expense in our Alberta Division, as taken from our Form S-309, was as follows:

	Total Marketing Expense	Cost Per Gallon
1. Tank Wagon	$ 13,300.33	.05¢
2. Trucks and Drays	4,415.71	.02
That is on the total gallonage of course		
3. Loaned Delivery Equipment	2,306.31	.01
4. Barrels and Packages	23,403.87	.09
5. Salaried Stations	104,533.19	.40
6. Commission Stations	441,431.09	1.71
7. Supervision	22,423.57	.09
8. Salesmen & District Supervisors	67,888.98	.26
9. Service Stations	54,445.19	.21
10. Office Staff and Expense	148,201.76	.58
11. Other Expense which I will deal with later	209,505.95	.81
TOTAL:	$1,091,855.95	4.24¢

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12. Total Miscellaneous Losses, such as Bad Debts, etc. 59,164.17 .23¢

and then we had

13. Total Miscellaneous Income 115,205,11 .45¢

14. Total Marketing Expense 1,035,815.01 4.02¢

and from that we deduct marketing gallonage, that is the gallonage shipped direct from the refinery to the customer for which we put through a credit note of 5¢ per barrel. It does not go through our distribution system.

15. Less Expense Eliminated) Gallonage) 26,516.29 .10¢

16. Net Direct Marketing Expense 1,009,299.72 3.92¢

Form S-309, from which the above figures are taken, does not allocate expenses between products. In arriving at the cost per gallon above referred to, our sales divisor is our total direct sales, all products in Alberta, but does not include "Eliminated Gallonage," i. e., tank car shipments from the Refinery direct to customers, or sales at the Turner Valley Oil Fields.

And in this connection I should mention that the S-309 by classification covers the Alberta Division; the consolidated net earnings and profits on products cover only the refineries of Alberta. Those are the figures to which Mr. McGrath has been referring, the Alberta figures, and are the difference of $15,120.14 between them, which which is accounted for by sales expense in the North West Territories which comes under the Alberta Division.

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Our marketing expense for white products for the yar 1938, as per our official form "Consolidated Net Earnings and Profits on Products," was as follows:

Gasoline	-	3.42¢ per gallon
Refined Oil	-	3.46¢ " "
Distillate	-	2.54¢ " "
Average White Products		3.38¢ " "

In other words, our form "Consolidated Net Earnings and Profits on Products," breaks down marketing expense by products, whereas our Operating Form S-309 breaks down marketing expense by classifications. The following comments deal in detail with expense figures taken from Form S-309:

(Go to Page 9290)

1. & 2. Tank Wagon and Dray Expense:

This includes the cost of operating motor equipment which the Company owns which is principally in service in the Cities of Calgary and Edmonton. The cost per gallon on deliveries made by our tank wagons is .30¢ per gallon; the cost per gallon made on deliveries made by our stake trucks is 1.61¢ per gallon. A good deal of money has been saved by not operating company equipment at country points. Substantial economies in our marketing expense have been effected by our policy of financing agents to buy trucks whereby the agent assumes all expense in connection with same. The agent can also use his trucking equipment for outside work to supplement his commission earnings at our smaller agencies and thus make it possible for him to make a livelihood. We have 242 commission agents in Alberta who own motor equipment, and therefore, in a position to make deliveries to dealers and farmers. As of December 31, 1938, there was an unpaid balance on 88 trucks of $34,243.79, of which payments of only $120.00 were in arrears.

3. Loaned Delivery Equipment Expense:

You will note that our total expense in 1938 for Loaned Delivery Equipment was $2,306.31. Most of this is accounted for by loaned equipment to Aviation Companies in Northern Alberta. Substantial economies in our marketing expense have been effected by our policy of not loaning equipment to dealers, but selling them instead, their underground tanks and pumps on terms.

Throughout most of the United States, - conditions may have changed recently but over a period of 10 years the statement is true, equipment is loaned to dealers which increases marketing expense and encourages new outlets. Therefore, our policy in Alberta of not loaning equipment, has

has served a two-fold purpose:

1. It has reduced marketing expense.

2. It has discouraged unnecessary new outlets.

4. <u>Barrels and Package Expense:</u>

It is obvious in Alberta that steel barrels are required in immense numbers to service the farmers. Up to the present we have been loaning barrels to farmers. We intend to carry on loaning the steel barrels we now have so long as they do not need replacement. When additional barrels are needed, it is our present intention to sell the farmers non-returnable barrels at cost. As of Dec. 31, 1938, the depreciated value of all our steel barrels in Alberta was only $19,104.06. Our steel barrels therefore, including maintenance, represent today a very small charge against marketing expense. On the other hand, the farmer enjoys the use of thousands of these barrels without having been put to the expense of buying them. At the present time a 15-gauge galvanized barrel of 45-gallon capacity costs approximately $8,35 laid down at Calgary. A 15-gauge lubricating black barrel of 45-gallon capacity,costs approximately $7.17 laid down at Calgary. As we have at present 94,680 steel barrels in Alberta, you can readily see what a tremendous investment on the part of the farmers for steel barrels would be required if they did not have all these barrels on loan from us. Many of our barrels loaned farmers are being used by local oil companies who have thus saved themselves the expense of buying these barrels to carry on their business.

5 . <u>Salaried Stations Expense:</u>

We operate salaried bulk stations at Calgary,

Edmonton, Lethbridge, Wetaskiwin and Ponoka. Our bulk stations at Calgary and Edmonton not only look after the requirements of the Cities in question, but a major portion of their expense is incurred in storing lubricating oils and filling same into barrels and cases ready for shipment to all points in Alberta. This also applies to shipment of other merchandise such as Grease, Atlas Tires, Atlas Batteries, etc.

During 1938 our Edmonton Plant stored, filled and shipped the following products:

Lubricating Oils - Barrels Filled:	10,874 Bbls.
Other Products - " "	22,711 "
Other Packages Filled:	4,110 "
Barrels Shipped:	36,799
Other Packages Shipped:	42,904

Similar data covering the Calgary Plant is as follows:

Lubricating Oils - Barrels Filled:	13,162 Bbls.
Other Products - " "	16,153 "
Other Packages Filled:	516 "
Barrels Shipped:	37,453 "
Other Packages Shipped:	54,288 "

6. Commission Station Expense:

Our total expense for operating 279 commission stations in 1938 was $441,431.09, or an average of 2.19¢ per gal. Of this amount, $338,630,24 represents total commissions paid, or 1.68¢ per gallon. Commissions paid on White Products totalled $276,898.34, or an average of 1.499¢ per gallon. Commissions paid on Lubricating Oils and Greases amounted to $46,098.69, or an average of 4.56¢

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per gallon. Commissions paid on Light Fuel Oil Sales amounted to $6,933.13, or 1.03¢ per gallon. Therefore, exclusive of commissions, our total expense at all our commissions stations, including taxes, depreciation, maintenance and all direct charges of every kind, was $102,800.85, or an average of .51¢ per gallon.

We operate our rural agencies on commission because it is more economical for us to do so than to operate them on salary. We cite a few typical examples to illustrate:

Agency	Sales	Commissions	Cartage	Total	Estimated Comparable Expense if Salary Operated
Bonnyville	252,704	$2940.62	$1133.35	$4073.97	$4601.56
Lacombe	140,424	2334.37	315.08	2649.45	2935.21
Bashaw	107,987	1798.94	-	1798.94	2659.46
Burdett	34,187	711.28	-	711.28	1730.02

The above indicates that even at our larger commission agencies it is more economical to operate at present commission rates than to operate on Salary. At smaller points such as Burdett, salary operation is entirely out of line with our present commission costs. That is because our agents at these smaller points are mostly part-time men supplementing their commission earnings from other sources. There would be an average reduction of .50¢ per gallon in commissions if free deliveries to farmers were eliminated and the agent's commission reduced to 1¢ per gallon thereon. It is, however, our considered opinion - after having gone into the matter thoroughly - that the farmers demand free delivery of their products. Of course, free deliveries to farmers could be discontinued by legislation the

same as rural mail routes could be discontinued, but we are strongly of the opinion that such a policy would be viewed with disfavor by most farmers. After all the farmer is getting his products delivered at only 1¢ over the price which applies to undivided dealers who may buy from 10,000 gallons upwards in one year. Our commission agents in reality are retailing to farmers in 20-gallon quantities and upwards at only 1¢ over the price to undivided dealers. Our commission agent would find it impossible to make a living on a commission of 1¢ per gallon as truck equipment would then be required only for deliveries to dealers which the commission agent could not afford. Besides he would be deprived of the supplementary earnings that he is at present making by doing outside work with his trucking equipment and is thus able to carry on with a much lower commission than he otherwise could.

The prevailing rates of commission paid in Montana, according to our information, are as follows.

<u>White Products</u>

Up to 5 miles - 1¢ per Wine Gal. - or - 1.2¢ per Imp. Gal.
Over " " $1\frac{3}{4}$¢ " " " - or - 2.10¢ " " "

These commission rates apply on deliveries to both dealers and farmers. You will therefore note from the above figures that the prevailing commission rates in Montana are somewhat higher than those prevailing in Alberta.

If we discontinued making free deliveries to farmers in Southern and Central Alberta we would lose the gallonage to truckers operating out of Calgary who would continue to deliver free on main highways. Farmers who live

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on secondary roads would be the only ones who would have to call at the agency for their products.

Agents with trucks deliver oil products to the farmer and often take back wheat to the elevators, thus helping to finance the farmers during the threshing season. These agents' trucks also are of very real value in picking up empty steel barrels from the farmers and thus enabling us to get the maximum turnover from our steel barrel equipment.

If commissions were reduced to a point where we would not be able to secure commission agents, dealers would then have to supply farm business and provide adequate storage for which they would expect and probably secure a discount equivalent to the commissions we now pay. Undoubtedly some companies trucking out of Calgary today are giving the dealers a discount to go after farm business instead of appointing commission agents. In that case the discount is not included in their marketing expense but comes off the price they realize. In other words, if we discontinued our present system of commission agencies and substituted instead, dealer distributors in each town to service the farmers, we would be merely transferring present commission expense over to a discount in prices.

Exclusive of commissions our total direct expenses for operating all our commission agencies in 1938, amounted to $102,800.85, or as before mentioned, an average of .51¢ per gallon. Of this amount, $48,581.76 represents depreciation, and $21,663.28

represents taxes, leaving a balance of $32,555.81 to defray all other direct expenses at our 279 commission agencies throughout Alberta. In this connection would point out that the amount of $32,555.81 above referred to includes $12,330.38 for moving storage tanks to new locations - principally in the area north of Waterways - leaving a net normal direct expense of only $20,225.43. Therefore, if we were to close one-third of all our commission agencies in Alberta, theoretical savings in depreciation, taxes and all other direct operating expense - exclusive of commissions - would be approximately $30,000 per annum. This saving would be far more than offset by very substantial increased transportation costs as we will deal with later.

Depreciated value of plant and equipment at 280 agencies in Alberta as of December 31, 1938, amounted to $292,033.77, or an average of $1,042.98 per agency. For this investment the Company not only provides unfailing service in every part of the Province, but also very materially reduces the transportation expense it otherwise would have to bear. The average rural retail dealer throughout Alberta has usually underground tankage of either 250 or 500 gallons capacity for one or two grades of Gasoline. In some cases he has underground storage of 1000 gals., capacity for the principal selling grade of Gasoline. In any event, his underground tankage is not generally sufficient to take care of farmer requirements. Therefore, to supplant our present system of distribution with underground tankage of sufficient capacity to meet requirements during the peak season would mean a new capital

expenditure in excess of depreciated value of our present plant, with the grave danger that deliveries during the peak requirements - especially if aggravated by bad road conditions - would be totally unequal to the demand. It is impossible to estimate what the loss in dollars to the farmers of Alberta would be if their threshing could not be completed before the rainy or winter season set in on account of a breakdown in fuel supplies.

Exclusive of main plants, we operated 267 bulk agencies as of Dec. 31, 1938. Our information is that at 129 of these agencies we have no competitor with above ground storage; at 79 points we have only one competitor with above ground storage; at 32 points we have 2 competitors with above ground storage. In other words, we operate only 27 commission agencies in Alberta where we have more than 2 competitors with above ground storage. We have not taken into consideration competitive agencies with underground storage as in most cases these are in reality, dealers with inadequate tankage to meet harvest requirements if located any distance from the Calgary Refinery. Undoubtedly the impression that there is over-duplication of bulk distribution facilities is caused by wrongly assuming that the situation that exists at central distributing points such as Lethbridge, Camrose, Red Deer, etc., prevails at all other towns throughout Alberta, which, of course, is not the case as the above figures reveal.

We have made a detailed study of what savings could be effected by closing our smaller agencies. With the exception of those located within convenient trucking

radius of the Calgary Refinery, our study indicates that savings would be offset by increased transportation costs. If we close such agencies we would then have to supply their requirements by truck from the nearest agency where the product in question was carried in bulk. The average cost for so doing would be 1/2¢ per gallon interstation commission plus 1¢ cartage, or a total added transportation cost of 1½¢ per gallon. We will cite a few examples to illustrate:

Our total sales of White Products at Therien amounted to 26,900 gallons in 1938. Total direct expense for rentals, taxes, depreciation, maintenance, was $134.67. If we closed this agency it would have to be supplied by truck from St. Paul at an interstation transfer expense of 1½¢ per gallon, or $213.32, or an increased expense of $78.65.

Our total sales of White Products at Mirror amounted to 45,116 gallons; total direct expense exclusive commissions, was $294.41. If the agency at Mirror was closed it would have to be supplied by truck from Bashaw at a total interstation transfer cost of $495.68, or an increased expense of $201.27.

Our sales at Innisfree for 1938 were 61,314 gallons. The savings in direct expense exclusive commissions, by closing this station of $266.21, would be offset by interstation transportation expense of $792.55, or an increase in expenses of $526.34.

Our sales at Sedgewick were 90,048 gallons. The savings in direct expense exclusive commissions,

by closing this station of $366.18, would be offset by interstation transportation expense of $1186.74, or an increase in expense of $820.56 per annum.

The direct expense - exclusive of commissions - for 1938 of $102,800.85 at our 279 commission agencies averaged $368.00 per commission agency. In other words, increased interstation transportation costs of 1½¢ per gallon on only 24,533 gals., would offset the average direct expense above referred to. However, the above comparison of savings to be made in direct expense by closing commission stations as against extra costs incurred for transportation, is not the whole picture by any means because in most cases we would have to provide underground tankage facilities in the town where we closed the agency unless the dealer did so at his own expense, and in either case he would demand and undoubtedly secure a discount to look after farm sales equivalent to present commission rates.

Even within reasonable trucking distance of Calgary there are many factors to be considered in withdrawing from our present sites on the railway and moving downtown. At some points within reasonable trucking radius of Calgary Refinery we have already transferred our 11½x20 storage tanks to points where trucking is not feasible. Therefore, our plant at these points in many cases is now only a 20x30 warehouse. We are trucking in barrel quantities direct from our Calgary Refinery to these 20x30 warehouses which, of course, is more economical than going to the expense of putting in underground storage within the town limits. However,

an understanding with the Railways will shortly have to be arrived at in this regard, because if trucking to these 20x30 warehouses located on railway property is prohibited, then we will have no alternative but to secure facilities downtown. Before rushing into such a move there are many factors to be considered such as cost of property down town, taxes thereon, cost of adequate underground storage, fire regulations and possible future regulations covering transport by truck.

As before mentioned, our total depreciated value on all bulk plants and equipment operated by our commission agents as of Dec. 31,1938, was only $292,033.77, or an average of $1,042.98 per agency. It is obvious that with such a low depreciated value in bulk stations it would be inadvisable to scrap our present plan for some other system of distribution that would entail a large new capital expenditure without corresponding savings to warrant same.

We have considered central distributing points such as Camrose, etc. It is, however, more economical to distribute direct to destination rather than to a central point and to re-distribute from there. For instance, the tank car rate from Calgary to Camrose is 3.12¢ per gallon as compared with 3.28¢ per gallon to Daysland, or a difference of .16¢ per gallon. To Tofield the rate is 3.28¢, or .16¢ per gallon over Camrose. Obviously, trucking from Camrose in competition with these differentials on through freights from Calgary is out of the question.

We have been for some time making a very detailed

study of our bulk station setup in Western Canada, but must keep in mind that if the Railways should decide to reduce their rates in order to meet trucking competition, it would alter the picture very materially. At points now supplied from Calgary by truck we can release a certain number of 11½x20 storage tanks for transfer to points where rail shipment is the most economical method of distrubution. To illustrate we will cite two examples:

Our existing one 11½x20 storage tank at Irracana can be transferred to Bonnyville for the storage of Esso at that point at a moving expense installed of $295.00 and would enable us to make an estimated transportation saving at Bonnyville of $395.50 per annum.

Our one 11½x20 storage tank at Langdon could be transferred to Faust for the storage of 3 Star Gasoline at an estimated moving expense of $285.50, with an estimated annual transportation saving at that point of $372.50.

There are other points in Northern Alberta to which such tankage could be transferred where the annual savings would more than pay for the moving expense installed, within one year. Our 11½x20 storage tankage in the field has also enabled our Calgary Refinery to ship in requirements in advance of the peak demand and thereby reduce investment in tank cars and tankage at the Refinery. We contend, therefore, that we do not have any unnecessary investment in bulk plants in Alberta as any tankage released in the Calgary area by virtue of trucking direct into underground tankage can be transferred to other points in Northern Alberta where tankage would be warranted by savings in transportation.

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7. Supervision Expense:

Until January 1, 1937, we operated two divisions in Alberta - one division for Southern Alberta with Calgary as head office, and one division for Northern Alberta with Edmonton as head office.

On January 1st, 1938, we consolidated both these divisions into one Alberta Division with head office at Edmonton. We reduced the supervisory staff to one Manager and two Assistant Managers for all of Alberta which is certainly the minimum to properly supervise our business. Under Supervision is included travelling expense, etc., for our Management.

8. Salesmen and District Supervisors' Expense:

The duties of salesmen include appointing agents and properly educating and supervising them in the conduct of our business. They also solicit dealers and large consumer accounts for the various products we handle, including Atlas Tires, Batteries and Accessories. They also supervise our service stations as well as solicit business from wholesale accounts and industrial accounts throughout the Province. They also assist our Auditors in auditing stations during the rush periods, and in general, are kept very busy on what we consider necessary work.

A substantial portion of the salesman's expense is travelling expense, as to get around the territory with dispatch, they operate automobiles which are company-financed. We advance the salesman up to $600.00 for the purchase of his automobile, repayable in 24 equal monthly installments. The salesman pays all expenses in connection with same for which he receives a mileage allowance of 6¢ per mile in the Cities of Calgary and

Edmonton, and 8¢ per mile on rural territories.

The title "Salesman" is misleading because in reality a large portion of the salesman's time is taken up in supervising our agencies and therefore, recently we changed their title from that of "Salesman" to that of "District Supervisor." It would be obviously impossible to carry on our business efficiently throughout Alberta without adequate supervision of our agencies.

9. Service Station Expense:

Our total sales at all our service stations in Alberta for the year 1938, were as follows:

Gasoline	-	3,397,531 gallons
Motor Oils	-	78,437 "
Greases	-	8,942 "
No. Tires	-	3,899
No. Tubes	-	5,078
No. Batteries	-	1,204
Accessories	-	$17,084.

Our sales of Gasoline, by grades, were as follows:

Esso	-	35%
Imperial 3 Star Gasoline	-	54%
Third Grade Gasoline	-	11%

In 1938 our total direct operating expense against our service stations was $54,445.19, or 1.55¢ per gallon as compared with direct charges of 2.19¢ per gallon at our commission stations. We collected rentals from the tenants of our service stations in the amount of $2,290.76 in excess of all direct operating expense, exclusive of depreciation and taxes.

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Our service stations were erected as an outlet for our products, the same as our bulk stations, and we obviously do not expect them to market our products without some operating expense. It is sometimes erroneously assumed that all operating expense in connection with service stations is a charge against gasoline. A substantial portion of our service station investment in buildings and equipment as well as carrying expense thereon, are for oil and greasing facilities for the sale of our lubricants and greases, and also proper facilities for the sale of our tires, batteries and accessories. Therefore, it is only reasonable that service stations operating expense should be credited with profits on products that we sell other than gasoline.

(Page 9305 follows.)

On the other hand, if the tenants did not have proper facilities for lubricating and greasing services and for sales of auxiliary lines such as tires, batteries etc., they could not provide adequate service nor make a livelihood at the retail margins at present obtaining in Edmonton and Calgary. The motorists in the larger centres demand modern and complete service and do not want to buy their requirements from a curb pump or have to drive inside a garage. If we had not been prepared to give the motorist in the larger centres the kind of service he demands, other oil companies would have done so and we would have lost by now practically all our business in the larger centres.

We operate to give satisfactory service in all parts of Alberta, but until we built our service stations we were particularly vulnerable to competition in the main centres. The reason for this is that competition usually picks out the largest markets and makes an effort to get distribution by offering special inducements to the larger dealers at these main centres. These inducements are various such as buying motor equipment from the dealer in question - storing and repairing their trucks and automobiles at certain garages whose business they hope to obtain - loaned equipment - and many other special lease or price arrangements which results in the dealer buying at a preferred price which he does not pass on to the consumer.

At our service stations, however, we receive the undivided dealer's price, and therefore any operating expense is to a large extent offset by saving special concessions and expenses that otherwise would have

been necessary to hold the dealer gallonage in those main centres. Other compensating credits are lower delivery costs by tank wagon, better credit control, less sales solicitation and better merchandising.

For the reasons above outlined, our percentage of the dealer gallonage in Cities such as Calgary and Edmonton is relatively small as is indicated by the following figures covering our sales of gasoline for the year 1938:

Calgary City:

(a) Service Stations	1,499,499 gallons
(b) Our Sales to Dealers	169,190 gallons
(c) Our Sales to other Consumers	191,626 gallons
(d) Total:	1,860,265 gallons

Edmonton City:

(a) Our Sales to Service Stations	1,278,891 gallons
(b) Our Sales to Dealers	380,913 gallons
(c) Our Sales to other Consumers	132,789 gallons
(d) Total:	1,792,593 gallons

It is quite evident, from the above figures, that if we closed any substantial percentage of our service stations at Calgary and Edmonton we would take a heavy loss in sales which would actually raise our cost per gallon for doing business in the Cities in question, because overall operating charges could not be correspondingly reduced. For instance, a saving of 10% in direct service station expense when accompanied by a loss of 10% in sales, results in a higher cost per gallon for doing business because general expense would then have to be applied to a smaller gallonage. Besides, if there is any profit in the sales of gasoline, lubricants, tires, greases, etc., we would also sacrifice such profits. This is something we are

forced to keep continually in mind when contemplating closing any existing service stations or bulk stations, because any ill-considered changes on a substantial scale in our present method of distribution might readily result in higher marketing cost per gallon, whereas our continual objective is ways and means of operating at a lower cost per gallon.

As of December 31, 1938, we had in Alberta, 31 service station locations on which we have not built. Fifteen of these sites are located in Calgary; ten in Edmonton, and six at other points. Our total investment in these sites is $263,111.48, and I might mention that 10 of them we acquired from the Regal Oil Company. We are not including this investment in our total capital employed in marketing operations in Alberta on which we are entitled to expect a return.

Our total carrying charges in 1938 on these properties were: For taxes $8,389.49; for maintenance $876.59, which less revenue of $5,077.36 received in the way of rentals, leaves a net expense on these properties of $4,188.72, for the year ending December 31, 1938. Our viewpoint is that this net expense of $4,188.72 is not an expense that should be charged to Alberta marketing. We consider these unused properties as an investment, the same as the purchase of bonds, which in no way should enter into our Alberta operating picture insofar as investment and expenses are concerned. In other words, the consumers of Alberta are in no way paying for these unused properties, but on the other hand, the Municipalities in question are the recipients of taxes promptly paid and the original owners of the property have no doubt by this time,

re-invested or spent the purchase price within the Province of Alberta.

Subsequent to the purchase of these properties, we took over the Regal Distributors on a merchandise account and acquired in this transaction 24 service stations, 4 of which have been closed; 1 leased to the Maple Leaf Petroleum, Limited, and the other 19 are now being operated by our tenants.

Since January 1, 1931, our company has only built 3 service stations in Alberta and during a similar period we have closed 6 service stations.

Service stations are usually attractively painted and are located on corner sites and therefore very conspicuous. They must of necessity be located usually on main thoroughfares. The above undoubtedly creates the impression that the duplication of service stations is much worse than it really is because for instance the cluster of service stations on a main street such as Jasper West, Edmonton, is not at all typical of the Cities of Calgary and Edmonton as a whole, or of the Province. For instance, beyond Jasper Avenue and 124th Street, there are practically no service stations, although a very substantial portion of the motorists in Edmonton live either West or North of this intersection. However, in going to and fro downtown Edmonton, the motorists use Japser West as their thoroughfore and for that reason service stations located in this vicinity can cater to a much wider clientele than if located on less important thoroughfares.

Our total direct operating expense for 1938 for all our service stations in Alberta of $54,445.19 was equivalent to .21¢ per gallon on our direct

sales of White Products. In other words, if we eliminated all our service stations in Alberta and held all the gallonage they now market, an impossible assumption, the reduction in marketing costs would only be approximately 1/5 cents per gallon and not several cents per gallon as is sometimes assumed. If we closed one-third of all our service stations in Alberta it would only mean a reduction in marketing expense of approximately $18,000.00, or .07¢ per gallon on our White Products sales. However, this saving would not materialize because in closing one-third of our service stations we would lose very substantial gallonage.

It is obvious that the price at which we can sell our products depends on our total cost of doing business in Alberta, which includes cost of raw materials, cost of manufacturing, transportation costs and marketing expense. If service station expense were entirely eliminated it would only reduce our total costs for doing business in Alberta by .91% and is therefore, contrary to popular belief, a very small factor in the total costs that determine the prices at which we can sell our products.

10. Office Staff Expense:

Our purpose in consolidating the Edmonton and Calgary Divisions into one Division as of January 1st, 1937, was to reduce office expense. We have endeavoured to simplify our system of accounting and cut down on office expense in every way possible short of reducing salaries. For instance, our commission agents are only being requested to mail us regularly, one report, namely, S-215 Cash Report. There are other reports occasionally required such as Form "S-172 Sub-Station Orders;

S-110 Tank Car Unloadihg Record. From time to time we may request special reports on collections, but the Cash Report is the only report sent us daily or weekly according to the size of the agency. We have also cut down statistics to those we consider absolutely essential in the intelligent guidance of our business, and therefore, a great deal of extra work had to be done in compiling data for this Royal Commission.

11. Other Expense:

Other Expense is expense that does not come under any of the classifications already referred to. Under this heading come expenses such as,

(a) Exchange	$6,161.15
(b) Legal Expense	5,422.72

$2500.00 of this amount was incurred in connection with collections.

(c) Employees' Annuities	4,154.35
(d) Death Benefits	5,273.73
(e) Group Life Insurance	1,137.15
(f) Licenses	7,136.84

Of this amount $7106.84 was for Fuel Oil License paid to the Province of Alberta.

(g) Taxes	13,107.80

Of this amount $8389.34 was for taxes on unused service station properties.

(h) Dealers' Expense Other than Rentals	8,473.07

We itemize this expense as follows:

Painting Dealers' Equipment & Premises:	$4,601.30
Maintenance of Dealers' Equipment:	1,686.32
Supplies:	1,256.40
Expense on Dealers' Identification Signs	645.06
Miscellaneous:	283.99
TOTAL:	$8,473.07

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On our total direct gasoline sales in Alberta for the year 1938, this dealer expense is equivalent to .046¢ per gallon, or less than 1/20th of a cent per gallon.

(i)

Rents Paid on Other than Service Station Properties:	$12,970.91

Of this amount, we paid rentals on dealers' premises as follows:

On 9 Third Party Leases:		$7,745.00
On 8 Cross Leases:		2,746.66
	TOTAL:	$10,491.66

As against the above rentals paid, we received rentals in 1938 as follows:

On Third Party Leases:		5,519.00
On Cross Leases:		1,380.00
	TOTAL:	$6,899.00

The difference between rentals paid and rentals received was therefore $3,582.66.

A Third Party Lease is where we lease the premises from a dealer and then re-lease same to someone else.

A Cross Lease is where we lease the premises from a dealer and then lease same back to him.

Our sales in 1938 in Alberta to the dealers in question amounted to 483,802 gallons of gasoline. The net rental absorbed of $3,582.66 was therefore equivalent to .74 cents per gallon. On our total direct sales of gasoline for Alberta it was equivalent to less than 1/50th cent per gallon. To summarize, our total expense for 1938 in connection with dealers' premises was as follows:

Painting, Maintenance & Supplies:	$ 8,473.07
Loaned Equipment:	2,306.31
Rentals Absorbed:	3,582.66
TOTAL:	$14,362.04

This is equivalent to .073¢ or approximately 1/14th¢ per gallon on our total direct gasoline sales in Alberta and indicates the small savings that would be accomplished by regulations. In addition to the above there is $12,404.42 as above referred to, covering depreciation on Identification Signs. These signs are made of porcelain and are good for many years to come and will soon be fully depreciated so that at that time they will cease to be an expense against marketing. However, we feel these signs have been well worth the expense from the standpoint of cementing our relations with the dealer, creating in him a pride in our products and identifying his place to the public as a place where Imperial quality products can be purchased.

(j) Advertising $36,343.19

This amount is made up as follows:

Radio	$9,176.60
50/50 Dealer Advertising	6,102.09
Newspapers	4,076.83
Posters and Banners	3,489.11
Printed Matter	2,268.69
Neon	1,422.40
Tourist Bureau and Maps	1,417.77
Motion Picture	1,182.40
Magazines	981.91
Portfolios	1,384.00
Programs and Donations	396.58
Display Racks	308.67
Imperial Dealer Magazine	1,826.99
Station and Dealer Signs	743.60
New Car Owner Campaign	699.57
Miscellaneous	865.98
TOTAL:	$ 36,343.19

Advertising is a controversial subject, but the most successful businesses in North America and Great Britian have come to the conclusion that judicious advertising is money well spent from the

standpoint of increasing sales or at least maintaining them. Increased sales that flow from public acceptance of our quality products due to judicious advertising, should assist us to reduce our marketing costs per gallon instead of the reverse. Our advertising expenditure for 1938 was equal to approximately one-half of 1% of our direct sales receipts and therefore it is evident that a very small decrease in sales receipts due to lack of consumer demand for our products would more than offset our advertising expenditures.

(k) General Administration $86,768.66

General Administration covers all head office expense such as, Executive Offices, General Sales Department, Treasurer's Office, Purchasing Department, Traffic Department, Safety Department, Tax Department, Legal Department, Secretary's Department, Annuities and Benefits Department, Technical Service Department, etc. These charges are allocated against each Province on the basis of direct gallonage, and Alberta for that reason does not bear an undue share. If all the functions performed by the highly trained personnel under General Administration were to be performed by Executives and staff located in Alberta, it would undoubtedly increase cost per gallon for those very necessary services.

12. Total Miscellaneous Losses: - $59,164.17

The principal items under this sum are,

Bad Debts Written Off:	-	$16,342.02
Bad Debt Reserve:	-	30,824.81
Cash Discounts:	-	5,179.58
Losses on Materials and Supplies	-	2,449.43

[illegible]

13. Total Miscellaneous Income: - $115,205.11

This includes items such as Bad Debts written off but subsequently collected, of $47,166.83; Rentals Received from other than our service stations, of $25,200.65; Commissions Collected, etc.

Our total direct marketing expense referred to up to this point, does not include Evaporation Losses, Sales Tax or Transportation Charges. We will therefore, deal with these three classifications briefly:

EVAPORATION LOSSES: Our evaporation losses incurred in the direct marketing of White Products for the year 1938 were .11 cents per gallon.

SALES TAX: The total sales tax paid in 1938 on products we marketed direct totalled $248,537.89. On White Products it amounted to .74 cents per gallon. This is a charge over which we have no control.

TRANSPORTATION CHARGES: In 1938 our transportation charges on direct sales in Alberta amounted to $1,279,719.27, as compared with our total marketing expense of $1,021,694.80. As previously pointed out in this statement, our transportation expense in 1938 would have been substantially higher than the above figure had we not been able to move a very large percentage of our products direct to destination in tank car quantities.

Our total expenditures in connection with our direct sales in Alberta for the year 1938 totalled $6,010,551.91 made up as follows:

[illegible]

Cost of crude and Raw Material	$2,642,847.13	43.97%
Freight	1,279,719.27	21.29
Sales Tax	248,537.89	4.14
Manufacturing Expense	653,528.83	10.87
Marketing Expense	1,021,694.80	17.00
Income Tax	164,223.99	2.73

Principal marketing items as taken from our Form 8-309 for the Alberta Division for the year 1938 represent the following percentages of the total expenditures of $6,010,551.91 above referred to:

Motor Equipment	$ 17,716.04	.29%
Barrels and Packages	23,403.87	.39
Salaried Stations	104,533.19	1.74
Commission Stations	441,431.09	7.34
Supervision and Salesmen	90,312.55	1.50
Service Stations	54,445.19	.91
Office	148,201.76	2.47
Other Expense	141,651.11	2.36

As mentioned before in this statement the price at which we can sell our products in Alberta depends on our total cost of doing business which includes cost of raw materials, manufacturing, transportation and marketing expense. You will note from the above that our total marketing expense on direct sales in Alberta only constitutes 17% of our overall cost. We are attaching herewith chart in this connection, which is self-explanatory.

This, therefore, concludes a review of our marketing operations in Alberta, particularly as they relate to marketing expense. In 1937 we reduced our marketing cost, as per Form 8-309, .85 cents per gallon.

Again in 1938 we showed a further reduction in marketing expense of .62 cents per gallon.

We are convinced that no radical departure from our present system of distribution is workable and if attempted, may defeat the very ends it attempts to serve. We do not take the position that further savings are impossible. We feel confident, however, that no marketing savings can be effected, with or without Government regulations, of such a substantial nature that it will enable us to reduce prices to a larger extent than we otherwise could in the normal unhampered conduct of our business. With increasing competition due to development of the Turner Valley Oil Fields, it obviously is a matter of self-preservation for us to continue our efforts to reduce our marketing expense so that we may on the one hand secure a fair return on our capital employed, and on the other, reduce prices to a point where we can maintain our position against any and all competitors no matter what their methods of distribution may be.

NOTE: Attached to and forming part of the above statement of this witness were the following documents, which are included here to avoid extending them as separate Exhibits:

AGENTS' COMMISSION AGREEMENT

I hereby agree to act as agent for Imperial Oil Limited, at ____________ to receive and unload into warehouse and distribute their petroleum and other products, and to account for same as required by Imperial Oil, Limited. I also agree to look after the general welfare of their business for, and in consideration of the following commission:

1. WHITE PRODUCTS:

1¢ per gallon.	To all dealers and Grain Companies, all methods of delivery.
2¢ per gallon.	To all farmers and consumers sold at posted tank wagon price,
	Inter-station commission 1/2¢ per gallon.

2. AUTOMOTIVE OILS:

Dealers and Industrial Accounts Under Contract		Farmers and Others at Open Market Prices	
Marvelube	- 5¢ per gal.	Marvelube	- 10¢ per gal.
Polarine	- 4¢ : :	Polarine	- 8¢ : :
Mobiloil	- 3¢ : :	Mobiloil	- 6¢ : :

3. OTHER LUB'G. OILS INCLUDING TRANSMISSION OILS, GREASES AND SPECIALITIES:

- 5% off the net invoice price.

Commission commences on Invoice S223 No. Tank Wagon S207 No.

In consideration of the above commissions, agent is to assume all expense in connection with the unloading of cars, handling full and empty barrels, and no further allowance will be made for cartage of any kind. Unloading tank cars, handling empty barrels , etc., etc.

It is understood and agreed that with the exception of those customers shown on the list of credit customers approved by________________office, all sales are to be for cash and the agent will be held personally responsible for any credit sales other than those mentioned above. He will also be responsible for credit sales to any customers for whom a "stop order" has been signed by him, until such times as a "lift order" is received.Agent will not be entitled to or receive commission on unauthorized credit deliveries. No commission will be allowed on charges to agents for stock shortages.

It is hereby expressly understood and agreed that the said agent shall be a trustee for Imperial Oil, Limited, for all monies including cash, cheques, promissory notes, stocks, bonds, mortgages, debentures and goods, or of anything of value whatsoever received by the said agent for or on account of Imperial Oil, Limited, under the contract, and that all such monies, including cash, cheques, promissory notes, stocks, bonds, debentures, mortgages, or anything of value whatsoever, received by the said agent for or on account of sales made for Imperial Oil, Limited, under this contract shall be deposited within ________days to the credit of Imperial Oil, Limited, at the Bank of ___________ at______________or at a Bank to be designated by Imperial Oil Limited.

And without in any way limiting the generality of the foregoing, it is also further understood and agreed that the agent is, without exception, responsible as trustee for all stock and equipment shipped to him or received by him. The civil liability of the agent for stock shortage shall be computed at the list prices prevailing at the agency at the time the shortage is discovered. It is further understood and agreed that the agent shall not purchase any of such stock from Imperial Oil, Limited, without its written consent, unless the agent shall before taking or removing the goods proposed to be purchased out of the company's stock, make out the usual cash sale invoice to himself and deposit the full purchase price in the bank designated by Imperial Oil,Limited.

And without limiting the generality of the foregoing, agent further agrees that he is directly personally responsible for:

(a) The furnishing of small tools, such as saws, hammers, pliers, etc.

(b) For repairs covering reasonable wear and tear and damage, excepting only fire, lightning and tempest.

(c) To see that the premises are kept in a clean and orderly condition at all times.

(d) All drums in stock or in the hands of customers at his agency, and that he will obtain the signature of customers for all drums delivered to or returned by them and that he will keep a correct record of such transactions verified by customers' signatures and that he will collect when empty all drums outstanding in his territory.

And without in any way limiting the generality of the foregoing, Imperial Oil, Limited,, may deduct any and all losses occasioned by a breach of this agreement from any commissions due or subsequently accruing due to said agent, who hereby constitutes and appoints the said Imperial Oil, Limited, his attorney to make such deduction.

The agent further covenants and agrees with the company that he is fully aware of all dangers and risks of every nature and description arising either directly or indirectly from or in connection with the performance of this agreement, and in consideration of the company entering into this agreement and as a condition thereof, he, the agent, hereby voluntarily agrees to encounter all such dangers and risks and to assume full responsibility for the consequences thereof, and he, the agent, hereby absolves the company from all claims for damage of any nature whatsoever arising therefrom,

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

[illegible]

whether in performance of his duties under this agreement or otherwise, and hereby waives and relinquishes all claims or causes of action whatsoever in respect thereof.

THIS AGREEMENT may be terminated by one week's notice by either party.

IMPERIAL OIL LIMITED

Per________________________ ______________________________________
Agent

Age______________________________

Countersigned: Single______________________________

______________________ MARRIED______________________________
Manager

Widower______________________________

British Subject or Alien__________

Protestant or
Roman Catholic__________________

This AGREEMENT is not valid unless countersigned by the Manager or Assistant Manager.

THIS CANCELS ALL PREVIOUS AGREEMENTS

LEASE

THIS INDENTURE made the ______________day of__________ one thousand nine hundred and ________IN PURSUANCE OF THE SHORT FORMS OF LEASES ACT:

BETWEEN:

IMPERIAL OIL LIMITED, a corporate body having its head office at the City of Sarnia, in the County of Lambton, hereinafter called the Lessor;

OF THE FIRST PART:

- AND -

____

hereinafter called the Lessee:

OF THE SECOND PART.

WITNESSETH, that in consideration of the rents, covenants and agreements hereinafter reserved and contained on the part of the Lessee, the Lessor doth demise and LEASE unto the Lessee, subject to the conditions hereunto annexed and forming part hereof and evidenced by the signature of the Lessee, and of the terms and conditions of the Lease, if any, under which the Lessor now holds:

ALL THAT

TO HAVE AND TO HOLD the said demised premises for and during the term of______________to be computed from the________ day of___________and from thenceforth next ensuing and fully to be complete and ended.

YIELDING AND PAYING therefor yearly and every year, during the said term unto the said Lessor, its successors and assigns, the sum of _______________payable on the following days and times, that is to say:

the first of such payments to become due and be made on the

______________day of______________

Should the Lessor make any additions or improvements to the buildings, plant and equipment in or upon the said premises, the Lessee's annual rent shall be increased by an amount equal to ten per centum of the cost of such increase from the

date on which the said cost shall be notified to the Lessee, such annual increase in rental to be payable in monthly instalments together with the payments of rental above provided for.

THE said Lessee covenants with the said Lessor to pay rent

AND to pay all rates, charges, and taxes wherewith the land or any business conducted thereon may be assessed during the term of this lease or any renewal thereof.

AND to repair, reasonable wear and tear, and damage by fire, lightning and tempest only excepted;

AND the said Lessor may enter and view state of repair;

AND that the said Lessee will repair according to notice in writing, reasonable wear and tear, and damage by fire, lightning and tempest only excepted;

AND that he will leave the premises in good repair, reasonable wear and tear and damage by fire, lightning and tempest only excepted;

AND will not assign or sublet without leave in writing.

PROVIDED that the lessee may remove his fixtures.

PROVISO for re-entry by the said Lessor or non-payment of rent or non-performance of covenants;

PROVIDED that in the event of the fire, lightning or tempest rent shall cease until the premises are re-built, or, at the option of the Lessor these premises forthwith to become null and void, and the premises hereby leased to be surrendered forthwith to the Lessor.

THE said Lessor covenants with the said Lessee for quiet enjoyment.

IT IS MUTUALLY AGREED that these presents are executed by the Lessor upon the express condition that the Lessee will purchase from the Lessor and no other, for re-sale on the

premises during the term hereby created, all the Lessor's regular trade mark brands of oil and petroleum and other products manufactured, dealt in, and/or sold by the Lessor, The Lessee agrees to pay the Lessor cash on delivery for gasoline at the Lessor's tank-wagon market price, and for all other products, the Lessor's dealer's price, cash on delivery, which prices may be current at the time of each purchase.

If the Lessee at any time fails, refuses or neglects to perform any of the conditions, stipulations or agreements herein contained which on his part ought to be performed, or shall become bankrupt, or have a petition in bankruptcy filed against him, or shall make any composition with or assignment for the benefit of his creditors, or shall permit any execution to be levied upon his goods, then and in any such case, the Lessor (in addition to any right or remedies heretofore conferred upon the Lessor)or its agents or Manager, or any other person authorized by it on its behalf, shall be at liberty to give fifteen days' notice of the termination of this Lease and forthwith, upon the expiry of the said fifteen days from the mailing of the said notice or the delivery of the same to the said Lessee , this Lease shall be determined and at an end and the Lessor may thereupon enter into and take possession of the said premises. Nothing herein contained shall be deemed or construed to make the Lessee agent of the Lessor, and the Lessee covenants and agrees to indemnify and save harmless the Lessor from all loss, costs, damages and expenses arising out of the existence of these presents or of anything done or maintained hereunder.

PROVIDED that the Lessor may terminate this Agreement at any time by giving the Lessee thirty, 30, days' notice in

[illegible] returns [illegible]

[illegible] some [illegible] petition [illegible]

[illegible] compensation [illegible]

[illegible] the benefit [illegible]

execution [illegible]

[illegible] the second day [illegible]

writing of its intention so to do, and at the expiration of the said thirty days the Lessee will quietly and peacefully deliver possession of the premises to the Lessor.

The covenants and agreements herein entered into by the Lessees where there are more than one are to be construed as both joint and several.

IN WITNESS WHEREOF the party hereto of the first part has caused its corporate seal to be affixed evidenced by the hands of its proper officers in that behalf and the party of the second part has hereunto set his hand and seal the day and year first above written.

SIGNED, SEALED and DELIVERED:)
In the Presence of:)

DISTRIBUTION of MARKETING and TOTAL EXPENSE on DIRECT SALES - PROVINCE of ALBERTA - 1938.

This Document is in the form of a graph, showing the following information:

83.00% made up of:

Cost of crude and raw material 43.97%

Freight 21.29%

Manufacturing Costs 6.56%

Mfg. Depreciation & Gen. Administration 2.46%

Packages 1.64%

Mfg. Taxes .18%

Sales Tax 4.14%

Income Tax 2.73%

[illegible]

A.E.Halverson

C2
21

Marketing 17.00% made up of:

Commission Stations 7.34%

Salaried Stations 1.74%

Supervision and Salesmen 1.50%

Service Stations .91%

Barrel and Pkg. .39%

Motor Equip. .29%

Office 2.47%

Other 2.36%

=============

DISTRIBUTION OF MARKETING & TOTAL EXPENSE ON DIRECT SALES

PROVINCE OF ALBERTA

Year 1938

		%
Motor Equipment	$17,716.04	.29
Barrel and Package	23,403.87	.39
Salaried Stations	104,533.19	1.74
Commission Stations	441,431.09	7.34
Supervision and Salesmen	90,312.55	1.50
Service Stations	54,445.19	.91
Office	148,201.76	2.47
Other	141,651.11	2.36
Freight	1,279,719.27	21.29
Sales Tax	248,537.89	4.14
Packages	98,598.10	1.64
Cost of Crude and Raw Material	2,642,847.13	43.97
Manufacturing Costs	394,510.89	6.56
" Depreciation and General Administration	149,808.94	2.49
" Taxes	10,610.90	.18

A.E.Halverson

C2
22

		%
Income Tax	164,223.99	2.73
TOTAL EXPENSE	$ 6,010,551.91	100.00

Toronto, Ontario,

May 17th, 1939.

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THE CHAIRMAN: Whatever conclusions we may come to about this report in the end, Mr. Halverson, we do want to express our appreciation of the great amount of work which has been put into it for our benefit.

A Thank you.

MR. NOLAN: May I speak to my learned friend? It has been suggested, Sir, that we go right along with the presentation of these various features of the marketing, and so with your permission, Sir, we will put in now as Exhibit "315" the "Price Structure" in Alberta.

THE CHAIRMAN; If the Witness is tired reading, Mr. Nolan, there is no reason why we should not take five minutes to give him a rest.

WITNESS: I am quite willing to go ahead, Your Lordship.

(DOCUMENT PRODUCED HERE MARKED AS EXHIBIT "315"

Q MR. NOLAN: Very good.

A The Imperial Oil Limited commenced marketing its products in Alberta in the year 1883. At that time we imported our products from the United States and for years thereafter our prices in Alberta were based on competition from others who might likewise import their products. In the year 1923 we built our Calgary Refinery.

With the discovery of substantial production of crude oil in Montana we were subjected to increasing competition from that source. On November 3, 1931, we acquired the Maple Leaf Refinery at Coutts. On December 15, 1933, we discontinued zoning our prices by areas and established instead, a posted tank wagon price

on 3 Star Gasoline of 20.5¢ Coutts - 22.5¢ Calgary - and 23¢ Regina. Our price structure on 3 Star Gasoline and other White Products in Alberta was then based on the posted tank wagon prices at these three points plus tank car freight to destination to the nearest one-tenth of a cent per gallon - lowest laid-down price to count. This established an individual price at each of our agencies in Alberta.

However, subsequent to December 15, 1933, we made numerous general price reductions in Alberta. On September 2, 1937, we reduced 3 Star Gasoline and Esso 1¢ per gallon. On November 22, 1937, we reduced 3 Star Gasoline and Esso 1½¢ per gallon. On January 5, 1938 we made a further reduction of 1½¢ per gallon on 3 Star and Esso.

Subsequent to acquiring the Maple Leaf Refinery, we supplied Southern Alberta with its requirements from Coutts. However, in the midsummer of 1937, due to increasing production of Turner Valley Crude, we began supplying Southern Alberta from Calgary Refinery. Therefore, on June 21, 1938, we discontinued basing our prices in Alberta on Coutts, Calgary and Regina - whichever was the cheapest - and based them on a posted tank wagon price on 3 Star at Calgary of 16½¢ plus tank car freight to destination, with the qualification that in Southern Alberta where Calgary prices plus tank car freight were higher than existing prices, we made no advance in price on account of Montana competition. This revised price structure resulted in a further average price reduction of approximately 9/10 cents per gallon on all products throughout Alberta.

The above is considered our normal price structure in Alberta at the present time, but in certain areas it has been necessary to put in temporary allowances on Acto Gasoline and Tractor Distillate to meet special competitive conditions, with which we will deal later.

In making any price reduction we must take into consideration the overall picture of our Alberta operations. If there are any reductions in cost such as crude oil, etc., we make an estimate of how many dollars per annum it will reduce our expenditures on our entire Alberta operations and then decide to what extent we are able to revise our price structure. Therefore, before contemplating any reduction we have to assure ourselves from the best estimates possible, that existing profits or reduced expenditures will warrant such a reduction. Whether or not we make the same reduction on all products depends on competitive and other conditions.

With this basic fact in mind when we made the last price adjustment, we made our calculations based on a posted tank wagon price of 16½¢ per gallon for 3 Star at Calgary, to which we added tank car freight to arrive at a price foreach agency in Alberta. We then determined in terms of 1937 sales what the reduction in dollars realized would be in Alberta if we put into effect this proposed price structure.

A. E. Halverson

We felt in making this computation that a posted tank wagon price of 16½¢ per gallon on 3 Star at Calgary - with a continuance of prevailing differentials on other White Products - was necessary on account of competitive conditions and also felt that as practically all our White Products are now supplied from Calgary, that the prices elsewhere in the Province should bear a direct relationship to Calgary plus tank car freight, providing estimated earnings warranted it.

Our figures at that time indicated that the reduction in question would reduce our receipts in Alberta on the basis of 1937 sales, by $295,747.00 per annum. If this figuration had indicated that the reduction was either more or less than our estimated earnings could stand, it would then have been necessary to make another figuration based on either higher or lower proposed tank wagon prices on White Products throughoutt Alberta.

(Go to Pagd 9331)

You will therefore note from the foregoing that contrary to what is sometimes assumed, our posted tank wagon price on Gasoline at Calgary and throughout Alberta is not based on so-called costs of each product ex Refinery. Such a basis is impracticable because in an extractive industry such as oil refining, there is no basis by which actual costs against each product can be determined except by arbitrary allocations, which after all is only an estimate. Even if such costs could be ascertained, a price structure has to be flexible enough to meet competition on the various grades of products produced from a barrel of crude, and on total operations, return a profit on capital employed.

The differentials on our other White Products sold in Alberta at the present time are:

Esso	-	2½¢ per gal.	over	3 Star
Royalite Kerosene	-	2¢ " "	"	3 Star
Acto Gasoline	-	2½¢ " "	under	" "
Heavy Tractor Distillate	-	3½¢ " "	"	" "

These differentials are not based on difference in estimated costs because it is impossible to make an accurate allocation of costs against individual products. Esso costs more than 3 Star on account of special base stock and higher octane rating, and also higher transportation costs due to less adequate tankage. Acto Gasoline on the other hand costs less than 3 Star because for instance, it contains no tetra-ethyl content, which in 3 Star Gasoline costs .87¢ per gallon. However, in determining differentials on our White Products we keep in mind two factors - namely - a return on our total operations in Alberta, and a different-

[illegible] such differentials [illegible] not

[illegible] contrary to that in competitive economy,

[illegible] prices on [illegible]

[illegible] based on severally [illegible]

[illegible]

[illegible] ability,

[illegible] agency [illegible]

[illegible] arbitrary allocations,

[illegible] Even if such costs

could [illegible] has to [illegible]

[illegible] grades of product

[illegible] of each [illegible] total operations,

[illegible] employ.

[illegible] differentials on our grade

[illegible] the present time are:

[illegible]	-	3½ per c.l. over 3 star
[illegible] Concessions	-	2½ " " " 3 star
[illegible]	-	2¼ " " under " "
[illegible] legislate	-	[illegible] " " " "

These differentials are not based

on differences in estimated costs because it is impossible

to me[illegible] effect of costs against individual

[illegible] more than 2 [illegible] on account of special

[illegible] in her cotton ratio, and also in her trans-

[illegible] less adequate technique. Into consider

[illegible] and are a [illegible] for instance,

it co[illegible] which [illegible]

[illegible] however, in determining differentials

[illegible] we keep in mind [illegible]

[illegible] operations [illegible] boards, [illegible]

A. E. Halverson

ial that is reasonably in line with competitive conditions. This principle also applies in the Oil Industry throughout the United States and other parts of the world.

We sell to farmers, products such as Acto Gasoline and Heavy Distillate satisfactory for production uses at very low prices. This is in line with out policy to sell the farmers the products they need for use in their tractors at the very lowest price possible. Therefore, in order to enable us to make some return on our entire operations, we endeavor to secure a somewhat higher price for our other products. The differential between products has to be reasonable, otherwise the low price product would supplant sales of the higher priced product to such an extent that the average realization would be reduced. We were the pioneers in introducing low priced products to the farmers for production uses when on June 9th, 1931, we telegraphed all our Prairie Managers as follows:

"Reduction in price of 5¢ per gallon on Tractor Kerosene "and 15% on Tractor Lubricating Oils will be made through- "out the Prairie Provinces effective June 10th. This "reduction is possible because of recent recessions in the "price of Crude Oil upon which the cost of all petroleum "products is predicated. As this recession in Crude Oil "prices would permit a reduction of only a fraction of a "cent on gasoline prices which it would be difficult to "extend to the consumer, it has been decided to extend "the entire benefit to the Western Farmer who is a large "user of Kerosene and Lubricating Oil for power farming "equipment. Unfavourable crop conditions and low prices

"still harass the Prairie farmer and the decision to "reduce prices of Tractor Kerosene and Tractor Lubricat-"ing Oil was reached in the hope that it would enable him "further to lower his operating costs and thus make a "larger margin upon the season's operations. This reduction "in prices will apply until the end of the threshing season "and as long thereafter as existing conditions prevail in "the petroleum industry. It is felt that the depressed "conditions maintaining in certain parts of the West "warrant this special accommodation for Prairie farmers."

This was followed by the introduction on August 1st of the following year, of Imperial Tractor Distillate at 5¢ per gallon below the posted price of 3 Star Gasoline. However, since that time we have steadily reduced the price of 3 Star Gasoline so that the differential to-day on Tractor Distillate is 3½¢ per gallon below the posted tank wagon on #3 Star Gasoline.

The basic principle of supplying farmers with Acto Gasoline and Distillate at low prices in an endeavor to reduce costs to the farmers is substantially similar to preferred freight rates on wheat. For instance, the Railways of Canada will ship a carload of wheat from Calgary to Edmonton for 20¢ per cwt., whereas the rate per cwt., on gasoline from Calgary to Edmonton is 39¢ per cwt. Insofar as the principle of a price structure flexible enough to meet competition is concerned, we again cite the Railways as an illustration: Last Winter Canadian Railways quoted a passenger rate of $168.50 from Vancouver to Los Angeles to New Orleans, to Florida, to Washington, to New York, to

[illegible]

[illegible]

[illegible]

[illegible]

Toronto, back to Vancouver, as against exactly the same rate from Vancouver direct to New York and return. Insofar as quality is concerned, apples grown on the same tree at the same cost, sell at different prices after being graded, because quality must be taken into consideration.

Throughout Canada the Esso differential is 2¢ per Imperial Gallon over 3 Star Gasoline, with the exception of Alberta, Saskatchewan, and Montreal, where the differential is 2½¢ per gallon. The reason the Esso differential is 2½¢ per gallon in Alberta as against 2¢ per gallon generally prevailing elsewhere in Canada, is that we felt the increased differential on Esso was justified to partly offset the low price at which Acto Gasoline is available in Alberta. The differential prevailing in the United States for Ethyl Gasoline is 2¢ per Wine Gallon or 2.4¢ per Imperial Gallon above the regular grade of gasoline. On the Pacific Coast it is 3¢ per Wine Gallon, or 3.6¢ per Imperial Gallon.

Our direct sales of Gasoline - exclusive of tank car sales - in Alberta for the year 1938 - were as follows, according to grades:

Esso	-	15%
3 Star & Premier	-	51.2%
Third Grade (Acto)	-	33.8%

Exclusive of Calgary, Edmonton and Lethbridge, the percentages were as follows:

Esso	-	10.2%
3 Star & Premier	-	50.2%
Third Grade	-	39.6%

Therefore, in making comparisons of prices with other Provinces in Canada, it should be kept in mind that in some of these Provinces we market none or very little Gasoline at less than the 3 Star price, whereas from the above figures you will note that 33.7% of our gasoline sales in Alberta in 1938 were at a price 2½¢ per gallon, or more, below the price of 3 Star Gasoline.

In making comparisons with United States prices it is sometimes overlooked by consumers that the Imperial Gallon sold in Canada is 1/5th larger than the Wine Gallon sold in the United States. It should also be taken into consideration that our selling prices in Canada include 8% Sales Tax, which in 1938 amounted to .74¢ per gallon on our direct gasoline sales in Alberta. The United States Government instead of a Sales Tax has a Federal Tax of 1¢ per Wine Gallon, which is not included in the selling price but added thereto. Therefore, our Sales Tax of .74¢ per gallon should be added to American prices to make them comparative with Canadian Prices. On this comparative basis, the prices at the present time in Montana - as per May 24th issue of National Petroleum News - are as follows, per Imperial Gallon, on a grade of Gasoline comparable to 3 Star:

Butte, Montana	-	16.94¢
Great Falls, "	-	16.34
Helena, "	-	17.54

On Third Grade Gasoline:

Butte, Montana	-	13.34¢
Great Falls, "	-	12.74
Helena,	-	16.34

There is no allowance off the above prices to dealers in Montana.

Professor Hardy of the University of Saskatchewan recently checked up on North Dakota prices and in evidence given before the Legislature of Saskatchewan, stated that "the tank wagon price of Green Gasoline in Crosby is 18.7¢ per Imperial Gallon. Plain Third Grade Tractor Gasoline costs 17½¢ in Crosby. Distillate costs 16½¢ per gallon in Crosby. Diesel Fuel Oil costs 13.8¢ per gallon at Minot."

Our posted tank wagon prices in Calgary, as you know, are: 16½¢ per gallon on 3 Star Gasoline - 14¢ on Third Grade Gasoline, and 13¢ on Distillate. From the above prices there is a discount of 1¢ to undivided dealers making the net price to dealers at Calgary: 3 Star Gasoline 15½¢ per gallon - Acto Gasoline 13¢ per gallon - Tractor Distillate 12¢ per gallon. From these prices there is also a temporary allowance of 1½¢ per gallon Acto Gasoline and 2¢ on Tractor Distillate.

In making comparison of prices with Montana and North Dakota, the relative consumption of gasoline per square mile should be kept in mind, as it is obvious that density of consumption and area to be served has a cital bearing on marketing and transportation expense. We therefore list herewith, certain statistics which are self-explanatory.

	Montana	Alberta
Area Square Miles	146,997	248,800
Motor Vehicle Registrations	173,892 (1937)	99,887 (1937)
Gasoline Consumption	113,840,000 "	65,823,379 "
Gasoline Consumption per Sq.Mile	774	265

Comparison with North Dakota:

	North Dakota		Alberta	
Area Square Miles	70,837		248,800	
Motor Vehicle Registrations	173,198	(1937)	99,887	(1937
Gasoline Consumption	121,741,000	"	65,823,379	"
Gasoline Consumption per Sq.Mile	1,719		265	

The above comparison is for the year 1937 as we do not have figures covering gasoline consumption in Montana or North Dakota for the year 1938. You will note from the above figures that the gasoline consumption for the year 1937 in the State of Montana was practically twice that of Alberta. Not only that, but the area in which it is sold is 40% less.

Therefore, in making comparisons with Montana prices, the lesser consumption and longer distances to be served in Alberta should be taken into consideration. In the year 1938 we materially reduced our marketing cost per gallon in Alberta due to an increase in direct sales of 17%. It is obvious that if Alberta consumption of petroleum products was twice that what it is, it would materially assist in reducing manufacturing, transportation and marketing expense per gallon.

Our direct sales of White Products in Alberta are sold at posted tank wagon prices, with the exception that to dealers and some large consumers, who purchase their requirements from us exclusively, we give a discount of 1¢ per gallon off the posted tank wagon price. In this connection we supplied as of Dec. 31, 1938, 700 dealers equipped with gasoline pumps. Of this number,

674 dealers purchased their requirements from us exclusively, and 26 dealers were divided accounts. In addition to the above, we supplied exclusively, 693 small dealers such as hardware stores, etc., who were not equipped with retail pumps with which to service the retail trade. As of Dec. 31, 1938, we supplied 305 consumers at the undivided dealer's price. Of this number, 127 consumers had underground storage.

The estimated percentage of White Products sold at undivided dealers' prices in Alberta for the year 1938, by principal brands, was as follows:

Esso	-	87%
3 Star Gasoline	-	72%
Acto Gasoline	-	48%
Distillate	-	18%
Average	-	65%

We table herewith as an exhibit, copy of our Exclusive Dealer's Agreement above referred to.

It is our considered opinion that the 1¢ per gallon allowance to dealers who buy their requirements from us exclusively, is warranted. It results in better credit control, lower delivery costs, less sales solicitation and minimizes substitution. It gives us an opportunity to work with the dealer to make him a better merchandiser of our products and by so doing, increases his sales, which, of course, indirectly increases our own. A farmer who buys in barrel quantities delivered free on his farm, in barrels loaned to him, is not entitled to as low a price as an undivided dealer who buys in much larger

quantities. We also have to take into consideration the fact that if we do not give dealers a better price than consumers, someone else would and we would merely lose the gallonage. This is particularly true of towns where we do not have an agency. The dealers at these towns demand a price which will enable them to supply requirements of the farmers in the immediate vicinity. Even at agency points we would likely lose the business of our dealers if we were to discontinue the 1¢ discount because truckers and others operating from Calgary would offer these dealers some kind of an agency deal which would be equivalent to the discount of 1¢ per gallon they are now securing from us as undivided dealers. Our average commission on White Products paid, indicates that approximately 50% of our sales at rural points are to dealers and therefore represents very substantial gallonage that we must protect against competitive inroads if we are to maintain our position in Alberta.

In this connection would advise that throughout Canada we have a similar policy of giving a discount of 1¢ off our posted tank wagon price on Gasoline to undivided dealers covered by an agreement, with the exception of Nova Scotia where the dealer's price is the posted tank wagon price.

We understand that in Montana the dealers purchase their requirements at the posted tank wagon price, but are informed that they must purchase their requirements exclusively from one company. In North Dakota and Minnesota the undivided edealer's price is 1.8¢ per Imperial gallon below the posted tank wagon price. In this connection might mention that in these two States, consumers who purchase 1000 gallons or more per month, are given the

undivided dealer's price. On the Pacific Coast, undivided dealers purchase their gasoline at 1.2¢ per gallon less than divided dealers. In Eastern United States the discount to undivided dealers is generally 6/10th¢ per Imperial Gallon below the posted tank wagon.

The total realization at Southern Alberta points based on 1938 sales below that which we would be obtaining if prices in this area were based on Calgary plus tank car freight, is as follows:

Grade:	Sales at Points Concerned	Amount	Average Per Gal.	Average Total Direct Sales
EssO	933,660	$ 2,525.63	.27	.08
3 Star & Premier	2,238,740	13,044.94	.58	.13
Acto Gasoline	1,187,200	11,548.50	.97	.18
Tractor Distillate	359,660	4,026.13	1.12	.33
Royalite Kerosene	215,565	1,256.21	.58	.11
Total Sales in this sub-normal area:	4,934,825	$32,401.41	.66	.15

The reason we are unable to secure in Southern Alberta our normal price structure of Calgary plus tank car freight, is because Montana Refiners are dumping gasoline into Alberta at considerably less than domestic prices charged in Montana. Our information is that American farmers and dealers pay the posted tank wagon price on "Q" Gasoline of 15.6¢ per Imperial Gallon at Great Falls, as against a price of 9.6¢ to Canadian Farmers, and 8.4¢ to Canadian Truckers. American farmers and dealers pay the posted tank wagon price of 12¢ per Imperial Gallon for Third Grade Gasoline at Great Falls, as compared with a

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price of 7.8¢ per Imperial Gallon to Canadian Farmers and Dealers and 6.6¢ per Imperial Gallon to Canadian Truckers.

If we are to continue selling products made from Turner Valley Crude in Southern Alberta, we will have to supply this market from the Calgary Refinery and continue to absorb freight losses. The only alternative is to abandon the Southern Alberta market to Montana dumping competition, or make arrangements ourselves to supply this market with products made from Montana Crude at Coutts.

Beyond reasonable trucking radius from the Calgary Refinery where we do not have bulk storage for a given product, we supply by truck from the nearest point at which we have bulk storage for such product. This means a higher laid-down transportation cost than if all products were delivered direct in tank car quantities from our Calgary Refinery. We list herewith, summary of transportation costs for Alberta in excess of costs by tank car, for the year 1938:

Grade	Total Direct Sales Alberta	Amount	Avge. Total Direct Sales
Esso	2,999,465	$15,617.52	.52 per gal.
3 Star & Premier	10,276,210	12,893.46	.13 " "
Acto Gasoline	6,780,025	10,798.07	.16 " "
Tractor Distillate	1,212,645	8,888.43	.73 " "
Royalite Kerosene	852,635	5,900.05	.69 " "
Total above Products:	22,120,980	54,097.53	Avge. .24

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[illegible] product.

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[illegible]	[illegible]	[illegible]	[illegible]

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The only way to reduce transportation charges in excess of tank car rates is by the installation of more tank car storage at our agencies, or where possible, to truck direct from the Refinery. Both these solutions are having our continual attention.

In certain areas it has been necessary to put in special allowances on Acto Gasoline and Tractor Distillate to meet special competitive conditions. What this amounts to for the year 1938 is listed below:

Grades:	Sales at Points Concerned	Amount	Avge. Per Gal.	Average Total Direct Sales
Acto Gasoline	3,154,845	$49,450.83	1.57	.77
Tractor Distillate	612,325	11,095.37	1.81	.91
Total Above Products	3,767,170	$60,546.20	1.61	.76

These allowances have been necessary to meet Montana competition in Southern Alberta, and in Central Alberta from competition of truckers drawing their supplies from Calgary and Turner Valley. Until we put these allowances into effect we were losing a substantial portion of our gallonage in these areas. Our posted tank wagon price is considered our normal price structure. As a policy, we scrupulously refrain from putting allowances into effect that are lower than competitive prices. Allowances, therefore, are not an offensive measure, but strictly defensive in order to protect our gallonage. If we are to serve all of Alberta at all seasons of the year, we endeavor to secure a normal price structure, but in certain areas of low

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[illegible]

[illegible]	[illegible]	[illegible]	[illegible]
[illegible]	[illegible]	[illegible]	[illegible]
[illegible]	[illegible]	[illegible]	[illegible]
[illegible]	[illegible]	[illegible]	[illegible]

[illegible]

[illegible]

cost marketing - or dumping competition - we must be prepared to maintain our position even if special allowances are necessary.

We summarize herewith, total deviations from our normal price structure in Alberta.

Brand:	Price Structure Less Than Calgary Plus T. C. Freight	Allowances Southern Alta.	Transportation in Excess of T.C. Rates	TOTAL Dollars	TOTAL Direct Sales Alberta	Avge. Per Gal. Alta.
EssO	$ 2,525.63		$15617.52	18143.15	2,999,465	.60¢
3 Star & Premier	13,044.94		12893.46	25938.40	10,276,210	.25
Acto Gasoline	11,548.50	49,450.83	10798.07	71797.40	6,780,025	1.06
Distillate	4,026.13	11,095.37	8888.43	24009.93	1,212,645	1.98
Kerosene	1,256.21		5900.05	7156.26	852,635	.84
Total:	$32,401.41	$60,546.20	$54097.53	147045.14	22,120,980	.66

You will thus note that our overall price structure in Alberta on the above products returns us an average of .66¢ per gallon less than the posted tank wagon prices. In addition to the above, we had as of Dec. 31, 1938, special price arrangements with 51 dealers. Total sales to these dealers in 1938 amounted to 1,224,328 gallons. The total amount of these price concessions was $8,834.50, or .72¢ per gallon on the gallonage involved. On our total direct sales of White Products in Alberta for 1938 it was equivalent to less than 1/30¢ per gallon.

Some dealers in towns where we do not have agencies had been requesting special prices to

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enable them to supply the farmers in their immediate vicinity. These dealers were very vulnerable to competition that would make them such offers. Therefore, in order to hold their gallonage on Esso and 3 Star Gasoline, we met the requests of these dealers half way by offering them a special allowance of 1/2¢ per gallon on only those products sold principally to the farm trade, i.e., Acto Gasoline and Tractor Distillate. Total sales on which the above allowance was made for 1938 amounted to 435,718 gallons, which at 1/2¢ per gallon totals $2,178.59.

On May 4th, 1937, we discontinued throughout Western Canada, posting retail prices at our service stations. Same is now entirely up to the tenants. However, our information is that to-day's retail margin over undivided tank wagon price in Calgary is 4½¢ per gallon, and in Edmonton 4¢ per gallon. At rural points it varies and is generally approximately 5¢ per gallon. A protection against higher retail prices at rural points is the fact that farmers can purchase gasoline at 1¢ over undivided dealers' prices in relatively small quantities to supply the requirements of their own motor equipment.

Retail margins at principal Cities throughout Canada are 4¢ per gallon, with the exception of the following:

Montreal	-	3½¢ per gallon
Regina	-	5¢ " "
Vancouver	-	5¢ " "

Figures taken from the Minerals

Year Book 1938 - Bureau of Mines, United States Department of the Interior, indicates that the average service station margin at 50 representative United States Cities in 1937 was 4.05¢ per Wine Gallon, or 4.86¢ per Imperial Gallon.

Apart from what competition may force us to do, we endeavor to maintain a sound relationship between overall costs and prices. For instance, if raw material costs decline - if prior to such a decline our prevailing prices have been in reasonable relationship to raw material costs - we will reduce prices. If no changes occur in raw material costs, we may reduce prices, if in our judgment competitive conditions so require. Naturally, we prefer to lose a certain volume of our gallonage rather than to hold it by dropping prices to a level that will entail a loss on all the gallonage. We do not make special price allowances unless we have evidence that substantial quantities of competitive products are being sold in the locality at prices below ours. If over a wide area our losses in sales are of serious proportions, we have no alternative to reducing prices regardless of costs. We cannot afford to allow too large a share of our business to go elsewhere because dwindling volume means increasing costs per gallon, both in manufacturing and marketing.

With the exception of payroll and commissions and the influence of volume, manufacturing and marketing costs are to a large extent, fixed charges, and so too are freights. About the only variable factor in costs for a given volume, is price of raw material such

as crude oil. Volume is an extremely important factor. The function of the Marketing Department is to endeavor to sell at reasonably profitable prices and to maintain volume. It is difficult these days to do both.

Some people may think that Imperial Oil Limited fixes the price at which gasoline and other petroleum products are sold in Canada. This is untrue. From time to time we adjust our prices to conform to operating economies, fluctuation in crude cost - or changing competitive conditions. It is our policy to tell anyone who wants to know - competitors or anyone else- what our posted prices are. We feel that price changes should be made openly - that we should not employ secrecy to gain temporary advantages, particularly when to do so would only result in confusion for dealers and consumers. There is no understanding that competitors must or should follow our prices. Presumably, large companies marketing over wide areas have costs somewhat similar to our own and cannot market profitably at lower prices than ours. If we reduce prices they have no choice but to follow if they wish to retain their gallonage. If we advance prices and they do not follow, we of course, will have to cancel the advance if we want to retain our customers.

The consumers of Alberta have benefitted very substantially in lowered price since the advent of the Turner Valley Oil Fields as a factor in Crude production. For instance, on Feb. 3, 1936, the posted tank wagon price of 3 Star Gasoline ex Calgary City was 23¢ per gallon as compared with today's posted

tank wagon price of 16.50¢ per gallon, or a reduction of 6½¢ per gallon. This reduction is also substantially true of the balance of Alberta. During a similar period, the decrease in prices of Gasoline - figures taken from the National Petroleum News - was 1.8¢ per Imperial Gallon at Great Falls, Montana, and .12¢ per Imperial Gallon at Minot, North Dakota.

We list herewith, index of weighted prices, in which prices prevailing in 1934 have been taken as representing 100:

		1938
Index Posted Tank Wagon Price 3 Star Gasoline at Calgary ..	-	73.3
Searle Grain Company's Index of Prices of Things Canadian Farmers Buy..................	-	110.5
Dominion Bureau of Statistics Index of General Level of Canadian Wholesale Prices ...	-	110.3

We attach herewith, chart in regard to the above which is self-explanatory. From same you will note that whereas wholesale prices in general have shown an increase of approximately 10% since 1934, Gasoline prices throughout Alberta during the same period, on the contrary, have shown a very substantial decrease. The decrease, for instance, in the posted tank wagon price of 3 Star Gasoline in Calgary since 1934, amounts to 26.7%

NOTE: Attached to and forming part of the above statement of this witness were the following documents, which are included to avoid extending them as separate Exhibits.

T-2
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A. E. Halverson

IMPERAIL
Dealer

AUTHORIZED BUYERS AGREEMENT

THIS AGREEMENT made in duplicate this .....day of.....193...
Between IMPERIAL OIL LIMITED, hereinafter called Company, and.......
.............................of......................................
(Street and Number)
....hereinafter Called
(City or town) (Province)
Buyer.

WITNESSETH:

In consideration of the covenants and agreements herein contained the parties hereto agree together as follows:

1. Buyer agrees to provide, on the above premises, underground tanks, piping, pumps and other facilities required for the delivery, storage and sale of Company's products sold to Buyer, and to use the same exclusively for such purposes during the life of this agreement.

2. Buyer agrees to purchase from Company all gasoline, kerosene, tractor distillate, oils, specialties and greases, antifreeze, and such other products as may be offered for sale by Company paying therefor for gasoline, kerosene and tractor distillate the Company's posted tank wagon prices current at the time of each such purchase, and for all other such products the Company's prices, terms and discounts current at the time of each such purchase, and that during the currency hereof no such products other than those of Company shall be sold or otherwise dealt with on or about said premises. Company agrees to sell such products to Buyer according to the tenor hereof.

3. Company agrees to make Buyer when not in default hereunder a special allowance of one cent (1¢) per gallon for all gasoline, kerosene and tractor distillate purchased from Company hereunder, such allowance to be made at time of payment.

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Provided however that in case of breach on the part of the Buyer of or default in any of the covenants and agreements herein contained, Buyer will without prejudice to any other rights of Company hereunder forthwith repay the whole sum of the special payment of one cent (1¢) per gallon allowed hereunder, and for the purpose of arriving at the said sum the amount of gasoline, kerosene and tractor distillate sold to Buyer up to the date of such breach or default according to the books of the Company shall be taken as final and binding.

4. Buyer shall not be responsible for failure to take delivery hereunder occasioned by strikes, accidents, fire or acts of God, and Company shall not be responsible for partial or total failure to deliver, or for delay in delivering directly or indirectly occasioned by acts of God, strikes, accidents, fire, transportation troubles or any other reason beyond its control, notwithstanding the provisions of Paragraph 5 hereof.

5. This agreement shall be and remain in force for...... ....from the date hereof, and shall continue from year to year thereafter, subject to termination after expiration of the said term of...........by either party giving the other written notice thirty days prior to the expiration of any year.

6. Company has and is hereby given the right to cancel this agreement any time on giving the Buyer ten days' notice of its intention so to do.

7. This agreement shall enure to the benefit of and be binding upon the parties hereto and their respective heirs, successors and assigns.

In the Presence of IMPERIAL OIL LIMITED.

....

....
(Buyer)

A. E. Halverson

PRICE COMPARISONS

1934 - 1938

Graph showing in graph from information contained in statements below:

A - IMPERIAL OIL INDEX OF POSTED T.W.PRICE THREE STAR GASOLINE AT CALGARY (1934 = 100.00)

1934 -	-	100.00	1937 -	Sept.	2	- 88.9
1935 -	-	100.0		Nov.	22	- 82.2
1936 -	Feb. 13	102.2	1938 -	Jan.	5	- 75.6
	June 13	97.8		June	21	- 73.3
	Sep. 21	93.3				

B - SEARLE GRAIN COMPANY INDEX OF PRICE OF THINGS CANADIAN FARMERS BUY (1934 = 100.00)

1934	-	- 100.0	1937 -	-	108.9
1935	-	- 100.6	1938 -	-	110.5
1936	-	- 102.4			

C - DOMINION BUREAU OF STATISTICS - INDEX OF GENERAL LEVEL OF CANADIAN WHOLESALE PRICES (1934 = 100.00)

1934	-	- 100.0	1937 -	-	118.1
1935	-	-- 100.7	1938 -	-	110.3
1936	-	- 104.2			

(At this stage the hearing was adjourned until 2:00 P.M.)

2:00 p. m. Session

A. E. Halverson.

MR. NOLAN: May it please you, Mr. Chairman, we have arrived now at the third part of the presentation of Mr. Halverson, and with the permission of the Commission, I will offer as Exhibit "316", "Jobbers' Prices & Sales - in the Province of Alberta."

(DOCUMENT IN QUESTION IS NOW MARKED EXHIBIT "316".)

JOBBERS' PRICES AND SALES - ALBERTA

Most of the Jobbers that purchase from us in Alberta purchase from us elsewhere in Canada and we have to keep this in mind in making quotations. Prices to Jobbers are established by letter from the Refinery Sales Department and are subject to change at any time, with the exception that supply arrangements with McColl-Frontenac Oil Company are covered by contract which runs to June 30th, 1939.

Buying in volume as they do, Jobbers are likely to make other arrangements if our prices are not satisfactory. For instance, in Alberta if they could not import to compete with our prices to them, then there is always the possibility they may build a Refinery at some point in the West such as Calgary or Regina, or may link up with some of the companies that have skimming plants in Turner Valley and who for this additional volume, would probably be willing to put in improved facilities for turning out quality products. Inasmuch as we already have a Refinery at Calgary capable of supplying this Jobbing business, this extra volume helps us to cut down manufacturing costs per gallon on our direct gallonage.

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Also, insofar as Refinery overhead is concerned, if we did not have this Jobbing business it would necessarily have to be a charge against our direct business. It might be contended that if we have surplus capacity at our Calgary Refinery to take care of this Jobbing business, that the Refinery capacity is in excess of our requirements, but on the other hand, if these Jobbers build their own Refineries, it is merely transferring overhead from our Refinery to the new Refineries.

There would be no purpose in our giving these Jobbers a better price than necessary simply to enable them to compete with as successfully, because we realize that Jobbing business is temporary, and direct gallonage is the only kind that can be considered reasonably permanent. For instance, at one time in Canada we supplied British American Oil Company; Sun Oil Company; Cities Service Oil Company; McColl-Frontenac Oil Company, and others, with their exclusive requirements, but we lost all or part of this gallonage overnight when they built Refineries or made other arrangements.

Our total sales to Jobbers in Alberta in the year 1938 were as follows:

Gasoline	-	13,918,473	gals.
Refined Oil	-	496,689	"
Distillate	-	1,034,877	"
Domestic Lubg. Oils	-	233,765	"
Imported Lubg. Oils	-	132,063	"
Light Fuel Oil	-	79,033	"
Bunker Fuel Oil	-	2,634	"
Asphalt	-	1,000	"
Greases	--	9,435	"
Turner Valley Naphtha	-	1,106,405	"

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Hereafter in this statement when we refer to White Products we are referring to Gasoline, Refined Oil and Distillate. Our prices on White Products to Jobbers during 1938, were as follows:

	Marginal basis below posted tank wagon price of products at Destination		
	Canadian Oil, Union, Hi-Way, Maple Leaf, North Star, Texas	McColl-Frontenac Oil Co.	
		Up to Jun.30, 1938	After July 1st
"Q" Colored Gasoline	6.00¢	6.75¢	6.50¢
Ethyl Gasoline	1.50¢ above "Q" Col.	7.50	1.50¢ above "Q" Col.
Stand.White Gasoline	.50¢ below "Q" Col.	7.25	.50¢ below "Q" Col.
Motor Gaso. (White)	5.00¢	5.00	5.50¢
Tractor Distillate	5.00	5.00	5.50
Tur. Valley Gasoline	5.00	5.50	5.50
Water White Kerosene	6.00	6.00	6.50

The above differentials are in effect at the present time, However, these differentials below the posted tank wagon price are somewhat misleading, as a large share of the sales made by the Jobbers are at undivided dealers' prices, i. e., 1¢ per gallon under the posted tank wagon.

We estimate that during 1938 the following percentages of White Products marketed by us were sold at undivided dealers' Prices:

Esso	-	87%
3 Star Gasoline	-	72%
Acto Gasoline	-	48%
Distillate	-	18%
Average	-	65%

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It is probable that the Jobbers' percentage of sales at undivided dealers' prices is higher than our own due to their having less non-dealer agencies. Therefore, our net average Jobbing differentials in Alberta for the year 1938 as taken from our statement "Consolidated Net Earnings and Profits on Products" for Alberta - which we will hereafter for brevity, refer to as our No. 9 Statement - were as follows:

	SELLING PRICE	FREIGHT	NET SELLING PRICE	Jobbers' Avge. Differential below our Selling Price
GASOLINE:				
Direct Marketing	18.70¢	3.85¢	14.85¢	
Jobbers	11.51¢	1.98¢	9.53¢	5.32¢
REFINED OIL:				
Direct Marketing	22.35¢	5.17¢	17.18¢	
Jobbers	14.72¢	2.37¢	12.35¢	4.83¢
DISTILLATE:				
Direct Marketing	15.25¢	3.62¢	11.63¢	
Jobbers	8.72¢	1.26¢	7.46¢	4.17¢

	TOTAL SAleS TO JOBBERS OF WHITE (PRODUCTS)	AVERAGE DIFFERENTIAL
GASOLINE:	13,918,473	5.32¢
REFINED OIL:	496,689	4.83¢
DISTILLATE:	1,034,877	4.17¢
TOTAL SALES WHITE PRODUCTS:	15,450,039	5.23¢

You will note that the Jobbers get a somewhat less differential on lower priced products such as Acto Gasoline and Distillate than they do on "Q" Brands. This is merely in conformity with our general price structure

whereby we secure on our direct business a lower netback to the Refinery on products that are principally used by the farm trade.

The average differential on White Products to Jobbers in 1938 was 5.23¢ per gallon below our direct selling prices, as compared with an average differential to Jobbers of 5.67¢ per gallon in 1937. You will therefore note that during 1938 the net differential enjoyed by Jobbers on White Products was reduced an average of .44¢ per gallon. From the average differential of 5.23¢ per gallon on White Products referred to, the Jobbers in question must -

1. Meet their marketing expenses.
2. Take care of transportation charges in excess of tank car rates.
3. Take care of inventory losses.
4. Secure some return on their capital invested and employed in marketing facilities.

In this connection would state that as of Dec. 31, 1938, we had - exclusive of unused service station properties - investment in marketing plant and equipment in Alberta at depreciated value of $1,733,717.34. In addition we had other capital employed representing Bills Receivable, Inventory, etc., totalling $1,491,199.27. None of this investment is necessary in connection with our Jobbing Sales.

Our consolidated Net Earnings and Profits on Products - No. 9 Statement - shows a profit of $73,891.06 on all Jobbing sales for the year 1938. However, this

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statement charges Depreciation, General Administration and Taxes at our Refinery of $75,740.72 against our Jobbing sales in Alberta. In other words, our Jobbing sales in Alberta not only showed a profit of $73,891.06, but also carried $75,740.72 of Overhead that would otherwise have had to be charged against direct marketing.

Further, our manufacturing costs per gallon in 1938 would necessarily gave been higher per gallon if the throughput through our Calgary Refinery had been radically reduced due to Jobbing gallonage being eliminated.

Therefore, our sales to Jobbers in Alberta for the year 1938 did not result in a loss that had to be recovered on products we marketed direct. The contrary is true. Not only did our Jobbing sales in Alberta in 1938 show a profit, but in addition they materially improved our position on our direct sales by carrying $75,740.72 of Refinery overhead as well as substantially reducing the manufacturing cost per gallon.

Q THE CHAIRMAN: Would you care to express any opinion now as to whether or not there would be advantage in eliminating the Jobbers entirely; not your Jobbers but all Jobbers, and having the refineries dealing directly with the people who are consuming their products. When I say "advantage" I mean from the standpoint of the consuming public, you being in exactly the same position as all your other Jobbers. You have pointed out in the Exhibit last filed, of course, you have to do business with these people because it may be that they would make other connections if you do not, and one follows that. What

A. E. Halverson.

I am putting to you, if you care to discuss it at this time and, if not, some later time will do equally well, is the larger problem, is there a necessity for Jobbers at all?

A It is a very great problem. If the number of oil companies doing business in Alberta were reduced in number - and that only could be done by Government edict or by prices so low that they could not afford to carry on - but however it is accomplished if it were done it would leave more gallonage for the remaining companies which, of course, would reduce their cost for doing business per gallon. How much I would not be able to estimate. It depends which jobbers were eliminated and what their gallonage was. But it is quite obvious if there were fewer companies doing business that the cost per gallon for doing business on the part of the remaining companies would be less. Probably not as substantial as is usually assumed.

Q What I am putting to you is not keeping some jobbers in and leaving some jobbers out, but I am just asking your opinion on the elimination of jobbers entirely, and the refinery dealing directly with those who consume your products. In short, the elimination of the middle-man, the old discussion, and I want to know your views as applicable to this industry as an experienced marketer?

A I am not quite clear in my mind that if we eliminated the jobber would he have the privilege of opening his own refinery. In that case nothing would be accomplished.

Q Well, of course, in that respect if it is advantageous to open a refinery I suppose anyone is at liberty to do that now. If they can see good business in it they will.

A. E. Halverson.

A If we were to shut off the jobber and discontinue supplying him and by that action compel him to build his own refinery, I believe it would increase the cost for doing business in Alberta instead of reducing it. There would be more duplication.

Q He would only go into the refining business though if he could do so at a profit, that is clear?

A Yes.

Q To himself. He is at liberty to do that right now, isn't he? You say you give him enough profit so he is deterred from doing it?

A We have a larger throughput in our refinery and probably a lower cost than he would have in a smaller refinery and he might find it to his advantage for the time being to buy from us and still give us a profit. If we refused to sell him a strong company such as the McColl-Frontenac, the Canadian Oil undoubtedly would make arrangements for a refinery of their own and would continue doing business. In that case it seems to me our cost would go up, and the cost generally.

Q MR. COMMISSIONER LIPSETT: Supposing, Mr. Halverson, that you gave that 5.23¢ that you now give on an average to the jobbers, would you not be in a much stronger position to increase sales?

A That was the point, Major, I was trying to cover. We could not give that price to the public because we have to take care of our marketing expense and the public is not being penalized so long as we make a profit on that business. In fact, our own business benefits because that jobbing business not only reduces the cost per gallon for

manufacturing the products we market direct, but it carries the overhead and if we lose that business our cost for doing the direct business would increase. Of course, we could not pass this jobbing price on to the consumer and distribute it through our warehouses all over the place. We have to provide for our marketing expenses.

Q Does the present system involve a double expense in the marketing, In the first place your marketing organization, and in the second place, the various jobbers' marketing organizations?

A As I said a while ago, Major, if there were less oil companies doing business our costs would be less because we would have more gallonage. But under the competitive system here they are doing business and we have to put up with them. So long as we can sell them and make a profit and reduce our costs we are glad to have the business.

MR. NOLAN: Now, with permission, Sir, we will put in the fourth part of Mr. Halverson's evidence, which is "Lubricating Oils. Sales, Distribution and Prices," as Exhibit "317".

(DOCUMENT IN QUESTION IS NOW MARKED EXHIBIT "317".)

Q THE CHAIRMAN: Before you go on, I notice here in the last Exhibit - I forgot to ask you at the time we were there - what is coloured gasoline?

A I am afraid I used a trade term. This "Q" coloured is a leaded gasoline with specifications comparable to 3 Star.

Q MR. FRAWLEY: 3 Star itself is a "Q" coloured gasoline?

A Yes.

A. E. Halverson.

LUBRICATING OILS

SALES, DISTRIBUTION AND PRICES

Our direct sales of Lubricating Oils in Alberta for the year 1938, were as follows:

Marvelube	634,562 gallons
Polarine	170,721 "
Mobiloils	119,443 "
Other Lubricating Oils	259,713 "
Total Lubg. Oils:	1,184,439 gallons.

Our direct sales of Greases were 1,101,322 lbs.

Our sales to Jobbers in Alberta for the year 1938, were as follows:

Imported Lubg. Oil	135,243 gallons
Other Lubg. Oil	230,585 "
Total Lubg. Oils:	365,828 gallons

Sales of Greases to Jobbers in 1938, in Alberta, amounted to 86,047 lbs.

Our direct sales of Motor Oils in 1938 in Alberta, i. e. Marvelube, Polarine and Mobiloil, totalled 924,726 gallons, of which 68.6% was Marvelube; 18.5% Polarine, and 12.9% Mobiloil.

We do not manufacture Lubricating Oils and Greases in the Prairie Provinces. All of our Lubricants are manufactured at our Sarnia Refinery in Ontario, with the exception of some Polarine and Industrial Lubricants which are manufactured at Ioco, British Columbia. In addition, we import Mobiloils and some other Lubricants from the United States.

We have tankage at Fort William for two grades of Polarine and three grades of Marvelube. We supply

A. E.Halverson.

this tankage at Fort William from Sarnia by boat.

Tank car shipments of Motor Oils into Alberta are made only to Calgary, Edmonton and Lethbridge, where we have lubricating storage to take care of tank car shipments. In addition, carload shipments from Fort William and Ioco are made to these points as well as direct to Waterways. In the year 1938, 23% of our Marvelube requirements were shipped into Alberta in tank cars direct from Sarnia; 65% were shipped in tank cars direct from Fort William, and the balance of 12% were shipped from Fort William in carload quantities. 21% of our Polarine requirements were shipped into Alberta direct from Sarnia; 71% from Fort William, and 8% from Ioco, British Columbia, 22% of our Mobiloil requirements were shipped into Alberta direct from Fort William, and the remaining 78% was shipped direct from the American Refineries at Olean, New York and Chaisson, Texas.

Within the Province of Alberta, carload shipments of Lubricating Oils and Greases are made from Calgary to Lethbridge, Brooks and Stettler, and from Edmonton to Peace River and Grande Prairie. With the exception of the above points to which carload shipments are made, the balance of our Lubricating Oils and Greases in Alberta are delivered from the cheapest supply point in less than carload quantities.

We have the same prices at all points in the Prairie Provinces for Marvelube, Marvelube Greases, Polarine and Mobiloil. We sell to farmers at list prices. Our list prices - with the exception of special grades - are as follows:

A. E. Halverson.

Marvelube	-	82¢ per gallon
Polarine	-	62¢ " "
Mobiloil	-	$1.20 " "

From these prices the dealer receives a maximum discount as follows:-

Polarine	-	10¢ per gallon
Marvelube	-	12¢ " "
Mobiloil	-	14¢ " "

In addition to the above discounts, the dealer receives an extra discount of 5% off the net invoice price providing he purchases his lubricating requirements from us exclusively. On carload quantities there is an additional discount of 2¢ per gallon, but no one seems to be interested in buying in carload quantities.

Our prices in Western Canada are only 7¢ per gallon above those prevailing in Eastern Canada on Marvelube and Polarine, and 10¢ per gallon above those prevailing in Eastern Canada on Mobiloils. Our average freight from Sarnia to Calgary is 12.52¢ per gallon. You will therefore note that Alberta enjoys favorable prices on motor oils as compared with other sections of Canada.

We attach herewith as exhibits, schedules of our list prices for Eastern Canada, as well as the Prairie Provinces. We also attach copy of our Exclusive Dealer's Agreement on Lubricating Oils.

We list on the following page, laid-down costs on Marvelube Motor Oil at 5 representative points in Alberta:

A. E. Halverson.

	Calgary	Edmonton	Lethbridge	Coronation	Grande Prairie
Cost - per Consolidated Net Earnings and Profits on Products, Alberta, 1938:	34.29¢	34.29¢	34.29¢	34.29¢	34.29¢
Sales Tax	1.48	1.48	1.48	1.48	1.48
Marketing Expense	11.88	11.88	11.88	11.88	11.88
Cost of Package	4.50	4.50	4.50	4.50	4.50
Total Cost Excl.Freight	52.15¢	52.15¢	52.15¢	52.15¢	52.15¢
Freight	12.52	12.52	12.17	19.20	19.09
Laid-Down Cost	64.67	64.67	64.32	71.35	71.24
Dealer Minimum Price	66.50	66.50	66.50	66.50	66.50
Tractor Owner Price	82.00	82.00	82.00	82.00	82.00

The costs in question have been taken from our 1938 statement "Consolidated Net Earnings & Profits on Products," for the Province of Alberta. You will note from the above statement that the marketing expense charged to Marvelube is 11.88¢ per gallon, of which commissions alone equal 5.35¢ per gallon. This average commission rate indicates that 93% of Marvelube sales at commission points are made to dealers. In Calgary and Edmonton practically all our Motor Oil sales are to dealers. In addition to this average commission of 5.35¢ per gallon, there are many other marketing expenses in connection with the sale of motor oils. For instance, when tank car shipments of same are received at Calgary and Edmonton, they must be put into storage tanks and then filled into barrels which have been properly cleaned and

painted. A large percentage of our motor oils are then trucked to the freight sheds and shipped at local rates to all points in Alberta. The barrel containing the lubricating oil is loaned to the customer and when empty, we must return same at local rates to supply points such as Calgary, Edmonton or Fort William for refilling.

Marvelube is a quality product which requires special equipment at Sarnia that is not necessary in the manufacture of ordinary motor oils and lubricating oils. This special equipment includes a phenol plant which cost $626,000 and a centrifuge plant which cost $219,000, or a special investment of $845,000.

Our statement "Consolidated net Earnings and Profits on Products," for Alberta, for the year 1938, shows that the average selling price of Marvelube at destination was 73.40¢ per gallon, from which must be deducted average freight of 16.79¢; marketing expense of 11.88¢ per gallon; sales tax of 1.48¢ per gallon, and cost of packages at Refinery of 4.50¢ per gallon, leaving a netback to our Sarnia Refinery of 38.75¢ per gallon. After deducting total costs of Marvelube of 34.29¢ ex Sarnia, this leaves us for the year 1938 - after deducting income tax of .98¢ per gallon - a net profit on Marvelube of 3.48¢ per gallon.

We do not have any breakdown of costs for Polarine and Mobiloil. Same are included under the sub-headings of "Other Lubricating Oils" and "Vacuum and Other Purchased Products," respectively, on our statement "Consolidated Net Earnings and Profits on Products." To make a separation for Polarine and Mobiloil from the sub-headings above

referred to would require going through every individual invoice and every individual freight charge for the year 1938.

Our direct sales of "Other Lubricating Oils" for the year 1938, by principal grades, were as follows:

Polarine	-	170,721 gals.
Railway Journal & Engine Oils	-	69,250 "
Steam Cylinder Oils	-	49,160 "
Machine Oils	-	39,940 "
Black Oils	-	13,729 "
Specialty Oils	-	14,836 "
Other	-	24,746 "
TOTAL:	-	382,382 gals.

Our net profit on "Other Lubricating Oils" as listed above for the year 1938 was 4.04¢ per gallon.

Direct sales for the year 1938 of "Vacuum and Other Purchased Products," by principal grades, were as follows:

Mobiloils	-	119,443 gals.
R.P.M. Diesel Engine Oils	-	25,560 "
Vacuum D.T.E. & Engine Oils	-	9,279 "
Technical White Oils	-	4,953 "
Medicinal White Oils	-	4,486 "
Vacuum Steam Cylinder Oils	-	1,998 "
Other	-	2,776 "
TOTAL:	-	167,495 gals.

Our net profit on "Vacuum and Other Purchased Products" as listed above, for the year 1938, was 12.67¢ per gallon.

A. E. Halverson

Our profit statement for the year 1938 shows a netback on Marvelube to the Refinery of 38.75¢ per gallon. It is therefore obvious that Polarine Motor Oil has a very low netback to the Refinery because our prices to farmers and dealers on Polarine are 20¢ and 17.1¢ respectively, below the Marvelube price. The low prices at which we sell Polarine Motor Oil is in keeping with our policy of selling the farmer petroleum products for production pruposes at the very lowest possible cost.

We market Mobiloil to compete with other imported brands such as Quaker State, etc. In this connection, the earning statement of the Quaker State Oil Refining Corporation - who operate throughout North America - for the year 1937, may be of interest. According to their annual statement, their total net sales receipts were $30,482,122 on which they made a net profit of $1,029,250, or 3.3%. This indicates that a motor oil selling at high prices in volume does not net as high a profit per gallon as is generally assumed.

Although our price on motor oils to farmers is higher than to dealers, it should be borne in mind that a negligible quantity of our sales to farmers today is made in barrel quantities. Sales are made instead in smaller quantities such as 10-gallon lots, which our agent - and in many cases the dealer - sells to farmers at barrel price. In view of the fact that the farmers are buying their motor oils in such small quantities, an increasing portion of our motor oil sales to farmers is being made through our dealers for which, of course, we realize only the dealer's price.

A. W. Halverson

Our statement "Consolidated Net Earnings & Profits on Products," groups all grades of Greases under one heading, on which we made during the year 1938 a net profit of .88¢ per gallon, or approximately .09¢ per lb., less than 1/10 of a cent per pound. In other words, the net profit on Greases was very small.

We do not establish retail prices on Motor Oils. Same is for the dealer to determine. However, our information is that the average retail price per quart prevailing in Edmonton and Calgary, and most of the rural points, is:

Polarine	20¢ per quart
Marvelube	30¢ " "
Mobiloil	40¢ " "

Retail prices in Eastern Canada are generally the same as those that prevail in Alberta. Retail prices throughout Montana on comparable grades, are as follows, per Imperial Quart:

Polarine	24¢
Iso-Vis	30¢
Mobiloil	42¢

The price in Montana of standard grade motor oil comparable with Marvelube - such as Iso-Vis, sold by the Standard Oil Company, of Indiana, is as follows, in terms of Imperial Gallons:

A. E. Halverson

	MARVELUBE Ex Any Agency in Alberta	ISO-VIS MOTOR OIL, EX: Great Falls, Montana	Minot, N. D.	Minneap. Minn.
Price to Farmers	82¢	85.08¢	90.48¢	90.72¢
Net Price to Dealers	66½¢	65.88¢	71.28¢	71.52¢

	POLARINE Ex Any Agency in Alberta	POLARINE Standard Oil of Indiana, Ex: Great Falls, Montana	Minot, N.D.	Minneap. Minn.
Price to Farmers	62¢	69.48¢	75.28¢	75.12¢
Net Price to Dealers	49.4¢	50.28¢	55.68¢	55.92¢

The above indicates that prices in Alberta on Lubricating Oils manufactured in Canada are selling at or below American prices. This in spite of the fact that manufacturing costs and distribution expense is undoubtedly higher in Canada due to much smaller volume of sales and larger areas to be served.

OPEN DEALERS PRICES

(Western)

F.O.B. Warehouse Points:- Ontario (West of Fort William), Manitoba, Saskatchewan and Alberta.

There is an Imperial product designed for, and therefore suitable for every automotive lubricating need. The satisfaction the motorist derives therefrom depends upon your using the correct grade.

ENGINE OILS		PER GALLON							
		BULK		INCLUDES PACKAGE					
				DRUMS	LITHOGRAPHED CANS				
		Bbls.	Half Bbls.	10 Gallon	1.5 Gallon	1.4 Gallon	4-1/2 Gallon	6-1 Gallon	24 Quarts
Marvelube 10	S.A.E. No.10-10W	.82	.85	.90	.98			1.15	1.02
Marvelube 20	S.A.E.No. 20-20W	.82	.85	.90	.98			1.15	1.02
Marvelube 30	S.A.E. No. 30	.82	.85	.90	.98			1.15	1.02
Marvelube 40	S.A.E. No. 40	.82	.85	.90	.98			1.15	1.02
Marvelube 50	S.A.E. No.50	.82	.85	.90	.98			1.15	[illegible]
Marvelube 60	S.A.E No.60	.97	1.00	1.05	1.13			1.30	1.17
Gargoyle Mobiloil "Artic Special"	S.A.E. No. 10-10W	1.20	1.23	1.35		1.47		1.53	1.40
Gargoyle Mobiloil "Artic"	S.A.E. No. 20-20W	1.20	1.23	1.35		1.47		1.53	1.40
Gargoyle Mobiloil "A"	S.A.E. No. 30	1.20	1.23	1.35		1.47		1.53	1.40
Gargoyle Mobiloil "AF"	S.A.E. No. 40	1.20	1.23	1.35		1.47		1.53	1.40
Gargoyle Mobiloil "BB"	S.A.E. No. 50	1.20	1.23	1.35		1.47		1.53	1.40
Gargoyle Mobiloil "B"	S.A.E. No. 60	1.40	1.43	1.55		1.67		1.73	1.60
Gargoyle Mobiloil "Ultra Heavy"	S.A.E. No. 70	1.40	1.43	1.55		1.67		1.73	1.60
Polarine 10W	(10W)	.62	.65	.77	.80		.84		
Polarine 20W	(20W)	.62	.65	.77	.80		.84		
Polarine 30	S.A.E. No. 30	.62	.65	.77	.80		.84		
Polarine 40	S.A.E. No. 40	.62	.65	.77	.80		.84		
Polarine 50	S.A.E. No. 50	.62	.65	.77	.80		.84		
Polarine 60	S.A.E. No. 60	.72	.75	.87	.90		.94		

When shipments are made in barrels or half-barrels, packages will be charged extra at prevailing prices and will be credited at price charged if returned within one year in good condition, all freight charges prepaid to warehouse point from which shipment is made.

Prices shown for ten-gallon drums of Marvelube, Mobiloil and Polarine Oils include a non-returnable package for which no charge will be made and no credit allowed.

GEAR OILS (including Extreme Pressure Type and GREASES		PER POUND									PER GALLON	
		DRUMS			LITHOGRAPHED CANS						LITHO. CANS	
		Bbls.	Half Bbls.	100 Pounds	1-25 Pounds	6-10 Pounds	1-10 Pounds	6-5 Pounds	24-1 Pounds	24-1 Pounds (Tubes)	1-5Gal.	6-1 Gal.
Marvelube Gear Oil 80	S.A.E. No. 80	.09	.095	.10							.95	1.15
Marvelube Gear Oil 90	S.A.E. No. 90	.09	.095	.10							.95	1.15
Marvelube Gear Oil 110	S.A.E. No. 110	.09	.095	.10							.95	1.15
Marvelube Gear Oil 160	S.A.E. No. 160	.09	.095	.10							.95	1.15
Marvelube Expee Gear Oil 80	S.A.E. No. 80 E.P.	.13	.135	.14	.175						1.30	
Marvelube Expee Gear Oil 90	S.A.E. No. 90 E.P.	.13	.135	.14	.175						1.30	
Marvelube Expee Gear Oil 110	S.A.E. No. 110 E.P.	.13	.135	.14	.175						1.30	
Marvelube Expee Gear Oil 160	S.A.E. No. 160 E.P.	.13	.135	.14	.175						1.30	
Marvelube Chassis Lubricant	(No. 11)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube U-G Lubricant	(No. 22)	.12	.125	.13	.165	.16	.175	.18		.40		
Marvelube Universal and Wheel Grease	(No. 33)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube Waterproof Grease	(No. 44)	.15	.155	.16	.195	.19	.205	.21	.22			
Marvelube Gear Grease	(No. 55)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube Cup Grease Medium	(No. 66)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube Cup Grease Hard	(No. 77)	.09	.095	.10	.135	.13	.145	.15	.16			

MISCELLANEOUS AUTO OILS	Bulk Bbls.	Bulk Half Bbls.	1-5 Gallon	12-1 Quarts	
Shock Absorber Fluid 36	.70	.73	.90	1.40	Per Gallon Net
Flushing Oil	$.32\frac{1}{2}$	$.35\frac{1}{2}$	$.52\frac{1}{2}$	-	" " "
Penetrating Oil	.58	.61	.78	-	" " "

Barrels and half-barrels charged extra at prevailing prevailing prices, and will be charged at price charged if returned within one year in good condition, all freight charges prepaid to warehouse point from which shipped.

Imperial Oil Limited guarantees the above products to be uniform in quality, and at all times, up to their standard.

March 1st, 1938

OPEN DEALERS PRICES

(Eastern)

F.O.B. Warehouse Points:- Ontario, (Fort William East), Quebec, New Brunswick, Nova Scotia and Prince Edward Island.

There is an Imperial product designed for, and therefore suitable for every automotive lubricating need. The satisfaction the motorist derives therefrom depends upon your using the correct grade.

ENGINE OILS		PER GALLON							
		BULK		INCLUDES PACKAGE					
				DRUMS	LITHOGRAPHED CANS				
		Bbls.	Half Bbls.	10 Gallon	1.5 Gallon	1.4 Gallon	4-1/2 Gallon	6-1 Gallon	24 Quarts
Marvelube 10	S.A.E. No. 10-10W	.75	.78	.83	.90			1.09	.95
Marvelube 20	S.A.E. No. 20-20W	.75	.78	.83	.90			1.09	.95
Marvelube 30	S.A.E. No. 30	.75	.78	.83	.90			1.09	.95
Marvelube 40	S.A.E. No. 40	.75	.78	.83	.90			1.09	.95
Marvelube 50	S.A.E. No. 50	.75	.78	.83	.90			1.09	.95
Marvelube 60	S.A.E. No. 60	.90	.93	.98	1.05			1.24	1.10
Gargoyle Mobiloil "Arctic Special"	S.A.E. No. 10-10W	1.10	1.13	1.25		1.37		1.43	1.30
Gargoyle Mobiloil "Arctdc"	S.A.E. No. 20-20W	1.10	1.13	1.25		1.37		1.43	1.30
Gargoyle Mobiloil "A"	S.A.E. No. 30	1.10	1.13	1.25		1.37		1.43	1.30
Gargoyle Mobiloil "AF"	S.A.E. No. 40	1.10	1.13	1.25		1.37		1.43	1.30
Gargoyle Mobiloil "BB"	S.A.E. No. 50	1.10	1.13	1.25		1.37		1.43	1.30
Gargoyle Mobiloil "B"	S.A.E. No. 60	1.30	1.33	1.45		1.57		1.63	1.50
Gargoyle Mobiloil "Ultra Heavy"	S.A.E. No. 70	1.30	1.33	1.45		1.57		1.63	1.50
Polarine 10W	(10-W)	.55	.58	.70	.73		.77		
Polarine 20W	(20-W)	.55	.58	.70	.73		.77		
Polarine 30	S.A.E No. 30	.55	.58	.70	.73		.77		
Polarine 40	S.A.E. No. 40	.55	.58	.70	.73		.77		
Polarine 50	S.A.E. No. 50	.55	.58	.70	.73		.77		
Polarine 60	S.A.E. No. 60	.65	.68	.80	.83		.87		

Prices on Marvelube Oils in barrels and half-barrels shown above include a package which is not returnable for credit.

Prices on Mobiloils and Polarine Oils in barrels and half-barrels do not include a package. Package will be charged extra at prevailing prices and will be credited at price charged if returned within one year in good condition, all freight charges prepaid to warehouse point from which shipment is made.

Prices shown for ten-gallon drums of Marvelube, Mobiloil and Polarine Oils include a non-returnable package, for which no charge will be made and no credit allowed.

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GEAR OILS (including Extreme Pressure Type) and GREASES		PER POUND									PER GALLON	
		DRUMS			LITHOGRAPHED CANS						LITHO. CANS	
		Bbls.	Half Bbls.	100 Pounds	1-25 Pounds	6-10 Pounds	1-10 Pounds	6-5 Pounds	24-1 Pounds	24-1 Pounds (tubes)	1-5Gal.	6-1 Gal.
Marvelube Gear Oil 80	S.A.E. No. 80	.09	.095	.10							.95	1.15
Marvelube Gear Oil 90	S.A.E. No. 90	.09	.095	.10							.95	1.15
Marvelube Gear Oil 110	S.A.E. No. 110	.09	.095	.10							.95	1.15
Marvelube Gear Oil 160	S.A.E. No. 160	.09	.095	.10							.95	1.15
Marvelube Expee Gear Oil 80	S.A.E. No. 80 E.P.	.13	.135	.14	.175						1.30	
Marvelube Expee Gear Oil 90	S.A.E. No. 90 E.P.	.13	.135	.14	.175						1.30	
Marvelube Expee Gear Oil 110	S.A.E.No. 90 E.P.	.13	.135	.14	.175						1.30	
Marvelube Expee Gear Oil 160	S.A.E No.160 E.P.	.13	.135	.14	.175						1.30	
Marvelube Chassis Lubricant	(No. 11)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube U-G Lubricant	(No. 22)	.12	.125	.13	.165	.16	.175	.18		.40		
Marvelube Universal and Wheel Grease	(NO. 33)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube Waterproff Grease	(No. 44)	.15	.155	.16	.195	.19	.205	.21	.22			
Marvelube Gear Grease	(No. 55)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube Cup Grease Medium	(No. 66)	.09	.095	.10	.135	.13	.145	.15	.16			
Marvelube Cup Grease Hard	(No. 77)	.09	.095	.10	.135	.13	.145	.15	.16			
MISCELLANEOUS AUTO OILS		Bulk Bbls.	Bulk Half Bbls.	1-5 Gallon	12-1 Quarts							
Shock Absorber Fluid 36		.63	.66	.83	1.33	Per Gallon Net						
Flushing Oil		.25½	.28½	.45½	-	" " "						
Penetrating		.51	.54	.71	-	" " "						

Barrels and half-barrels charged extra at prevailing prices, and will be credited at price charged if returned within one year in good condition, all freight charges prepaid to warehouse point from which shipped.

March 1st, 1938 Imperial Oil Limited guarantees the above products to be uniform in quality, and at all times, up to their standard.

A. E. Halverson

AUTHORIZED BUYERS LUBRICATING OIL AGREEMENT

THIS AGREEMENT made in duplicate this ....
day of............., 193..... between IMPERIAL OIL LIMITED, hereinafter called Company, and...................................
...............................of...........................
(Street and Number)
....hereinafter called Buyer
(City or Town) (Province)

WITNESSETH:

In consideration of the covenants and agreements herein contained, the parties hereto agree together as follows:

1. Buyer agrees to purchase from Company all lubricating oils, specialties and greases as shall be sold or otherwise dealt with on said premises, paying for such products the Company's Open Dealers' Prices and terms current at the time of each such purchase and that during the currency hereof, no such products other than those of Company shall be sold or otherwise dealt with on or about said premises.

2. Company agrees to invoice each delivery of Company's branded automotive lubricating oils and greases to Buyer at its Open Dealer's Price less the following quantitiy allowance on:

Cents per Gallon	Cents per Pound
Marvelube Oils and Gear Oils.......	Marvelube Gear Oils......
Gargoyle Mobiloils.................	Marvelube Greases........
Polarine Oils......................	

3. Company also agrees to make Buyer when not in default hereunder a special allowance of five per cent (5%) off the net invoice price for all lubricating oils, specialties and greases purchased from Company hereunder, such allowance to be made at time of payment.

A. E. Halverson

4. Company reserves the right to advance or reduce at any time, open Dealer price for lubricating oils and greases. In the event of an advance in prices, Buyer shall be entitled to purchase within thirty (30) days after date of advance, a quantity at the old prices not exceeding his (its) average monthly deliveries during the preceding twelve (12) months.

5. It is understood and agreed by Buyer that any and all dispensing equipment, advertisements and signs that may be supplied to him (it) by Company will be used by him (it) for the sole purpose of dispensing and advertising the products of the Company; that these advertisements, signs and dispensing equipment will be used and displayed by Buyer only so long as Buyer keeps in stock the articles which they describe in such quantity as to Company may seem sufficient to meet the demand, and that all advertisements, signs and dispensing equipment furnished Buyer shall remain the property of Company and will be surrendered to Company by Buyer on demand at any time.

6. Buyer shall not be responsible for failure to take delivery hereunder occasioned by strikes, accidents, fire, or acts of God, and Company shall not be responsible for partial or total failure to deliver, or for delay in delivering directly or indirectly occasioned by acts of God, strikes, accidents, fire, transportation, troubles or any other reason beyond its control, notwithstanding the provisions of paragraph 7 hereof.

A. E. Halverson

7. This agreement shall be and remain in force for....................from the date hereof, and shall continue from year to year thereafter, subject to termination after expiration of the said term of .... by either party giving the other written notice thirty (30) days prior to the expiration of any year.

8. Company has and is hereby given the right to cancel this agreement at any time on giving Buyer ten (10) days' notice of its intention so to do.

9. This agreement shall enure to the benefit of and be binding upon the parties hereto and their respective heirs, successors, and assigns.

In the Presence of:	IMPERIAL OIL LIMITED
....	....
....	....
	Buyer

MR. NOLAN: That, Mr. Chairman, completesthe material which Mr. Halverson has prepared.

MR. FRAWLEY: Do you intend to ask Mr. Halverson any questions at all.

MR. PLOTKINS: I have some to ask.

MR. FRAWLEY: There was one matter which was brought out the other day by you, Mr. Plotkins. I do not intend to cross-examine Mr. Halverson or ask him any questions but I think we should clear that up.

THE CHAIRMAN: You do not intend to now or at any time.

MR. FRAWLEY: Oh now, now.

THE CHAIRMAN: I see.

MR. FRAWLEY: Mr. Plotkins was discussing with one of the witnesses the other day, Mr. McGrath I think, the price at which Acto is sold in Calgary and I must confess I was all confused about it and I thought I would take this opportunity of having you tell us something about that. We have filed here Mr. Stevens' posted tank waggon prices and I will ask you to look only at one point, Calgary, Acto has a posted price of 14, so the final price is 12½?

A That is right.

Q Now what other deductions of any kind to anybody are made at Calgary on that gasoline?

A There are no deductions of any kind made to farmers or consumers below that price, but the 100% dealer buys Acto at 14 cents less 1 cent, which is 13, and he also gets an allowance of 1½, which is 11½, which is the lowest price to dealers.

Q That is the service station dealer selling Imperial producuts undivided, would pay $11\frac{1}{2}$ for Acto in Calgary?

A Yes.

Q But the farmer-consumer coming in for a barrel of Acto at your bulk plant in Calgary would pay the 14 less ----

A $1\frac{1}{2}$.

Q Which would be $12\frac{1}{2}$?

A $12\frac{1}{2}$ cents net.

Q He would pay $12\frac{1}{2}$?

A And to my knowledge there is no exception.

Q Now then a dealer, a dealer coming in from outside, well it doesn't matter, well I will tell you, Mr. Plotkins, if you would not mind pursuing that and I think it may as well be straightened out right now, if there is any question about this Acto being sold at anything less than a net $11\frac{1}{2}$ to dealers and $11\frac{1}{2}$ to anybody else?

Q MR. PLOTKINS: Mr. Halverson, some two or three weeks ago we were notified, in fact we learned it through the Gas and Oil Products who notified our office that the Imperial had that morning instituted a further adjustment of 1 cent covering certain points immediately adjacent to Calgary and that is what Mr. Frawley is referring to. Possibly you can clarify that?

A Yes, I will be very glad to. First of all to clarify it, we would like to table with the Commission the allowances, the names of the points and the allowances at all points in Alberta and we will get that ready for tomorrow and I think that would be helpful because instead of one or two points you would have all of them but when we came through here about six weeks ago I believe it was, we were quite concerned

with all of the farmers coming in, who were buying Ex Calgary and our agents within 30 miles of here were not doing very much business, the farmer likes to come in and go to a show or bring in some livestock or what-not, and on the highways leading to Edmonton and, all the highways, there was somebody who was selling him gasoline at 11½ cents or 11 or as low as 10½, and we found some invoices as low as 10 cents, and therefore the problem faced us, whether we should adopt a similar policy of having wholesale outlets on the main roads leading North, South, East and West, where the farmer could come in and pick up products at our prices and scrap our agencies, which it would in effect have meant, or some other proposal that would safe-guard our agencies for the time being and so we decided that those agencies which were located within 30 miles of Calgary,, and I think there are 7 of them, at those agencies we put in a further allowance of a cent per gallon. The agent takes a reduced commission of half a cent per gallon and we stood the other half, so at those 7 points, which we intend to table along with all the others, the allowance today is 2½ cents per gallon and our purpose, right or wrong, was that we had these agencies and we think they will be needed sometime in the future and we wanted to keep them, we didn't want to close them out and we either had to put those agents in the position to hold the business or put in some distribution in the City of Calgary that would do it, and the average farmer does not want to go to the refinery to pick up his products, it is too far out, so the only way we could compete with that business was to put in wholesale outlets on the main roads leading out of Calgary, which we did. It is a duplication because we already had a distribution in the country.

Q MR. FRAWLEY: Let me understand then, Calgary then, there are some points, Airdrie would be one of those points?

A Yes.

Q Just let me understand?

A There are 7 points.

Q Airdrie I suppose is one of the points, could you mention them?

MR. STEVENS: I can let you have them now.

MR. FRAWLEY: Will you name them if you please.

MR. STEVENS: Airdrie, Crossfield, Irricana, Dalroy, Strathmore, Langdon and Okotoks.

MR. NOLAN: That statement, Mr. Chairman, was made by Mr. Stevens who is the supervisor in Alberta of the marketing branch.

MR. FRAWLEY: We will take it as coming from Mr. Halverson.

MR. NOLAN: I wanted the record to show who had spoken.

WITNESS: Well I am tabling it.

Q MR. FRAWLEY: Airdrie has a price of 15.1 less 1½, I mean in this posted list, Exhibit "257", that is 13.6, is it not; this is our Exhibit and take Airdrie, Acto has a posted price at Airdrie of 15.1?

A Yes.

Q Less 1 cent to an undivided dealer is 14.1, less 1½ on the Exhibit "257", the regular differential discount, is 12.6?

A That is right, net.

Q And then you have another cent off that, is that what I understand in the last few weeks?

MR. STEVENS: No, that is the total allowance of $2\frac{1}{2}$ cents from all.

WITNESS: That is net. My understanding is that the dealers do not get anything below that price, do they.

MR. STEVENS: The dealer receives off the posted tank waggon price 1 cent, if he is an undivided daler and in addition to that there is $2\frac{1}{2}$ cents allowance to considered dealers but to the farmer there is only $2\frac{1}{2}$ cents allowance off the tank waggon price.

Q MR. FRAWLEY: Let me understand, Airdrie, the posted tank waggon price, according to Exhibit "257" is 15.1?

MR. STEVENS: Correct.

MR. FRAWLEY: Every undivided dealer in Crossfield or in Airdrie gets 1 cent off, whether it is Acto or 3-Star or Esso?

A That is right.

Q That brings us down to 14.1, the posted price, which he ordinarily pays?

A That is right.

Q On Exhibit "257" there is a differential discount which has been there since the 8th of December last, of $1\frac{1}{2}$ cents?

A That is right.

Q So that he is now buying, we now have it down to 12.6?

A That is right.

Q And some weeks ago there was a further differential put in that is what I would like to get and is what?

A One cent.

Q So we have the Airdrie dealer buying it at 11.6?

MR. STEVENS: That is right.

Q MR. FRAWLEY: That is what I wanted to know?

A That is right, the Airdrie dealer 11.6 net and the Airdrie farmer 12.6 net.

Q That is the Airdrie farmer but we have the dealer at Airdrie, the undivided dealer at these 7 points, and we may deduct from the undivided dealers' prices at each of those 7 points, 2½ cents?

A That is right.

Q 2½ cents from the undivided dealer price at those 7 points?

A Yes, and would you like those.

Q Yes, I would like to have that, so take the posted price, we can take 3½ cents off the posted price to the dealer at these 7 points?

A Yes.

Q Now then Calgary, that is a different proposition?

A That is right.

Q That is a different proposition, so that that frankly is where I got confused, Calgary is not in it at all?

A No.

Q It is 14 less 1½ and that still stands at Calgary?

A That is right.

Q Except the undivided dealer gets another one cent?

A That is right.

Q MR. FRAWLEY: You think at this time it might be well to file those, have you enough copies?

A No, I did not know exactly what Exhibits I would be asked for but I am prepared to submit any Exhibits which you wish.

THE CHAIRMAN: The morning will do quite well, Mr. Halverson. The witness prefers to file it in the morning.

[illegible] that I wanted to

know?

What is right, the answer [illegible] get to the girdle

formed like it.

[illegible] but to leave the dealer as [illegible]

[illegible]

[illegible]

[illegible]

That is [illegible]

[illegible]

[illegible] like planes.

[illegible]

[illegible]

[illegible]

Yes.

[illegible]

That is right.

What is a different proposition, [illegible]

[illegible]

Except the unedited [illegible]

That is right.

Mr. Kelly: [illegible]

might be [illegible]

[illegible]

[illegible]

[illegible]

Mr. [illegible]

[illegible]

MR. FRAWLEY: Oh yes. In fact there may not be enough made at the moment.

WITNESS: If you wish to cross-examine further, Mr. Frawley, here is a copy which might be helpful to you. It shows the area in which we make allowances.

MR. FRAWLEY: Yes I understand.

MR. NOLAN: We have prepared one for Dr. Fry and we have another one which could be marked now as an Exhibit, from Mr. Stevens.

THE CHAIRMAN: Well there is no anxiety to put it in to-night, if that is all we are going to do, just to put it in. The witness is going to discuss it tomorrow I understand.

MR. FRAWLEY: Yes. Well have you anything more Mr. Plotkins?

MR. PLOTKINS: I would like to ask a couple of questions.

Q MR. PLOTKINS: Mr. Halverson, this Airdrie agent of yours has the gasoline shipped to him or does he come into Calgary and get it?

A I would imagine he comes in because most of our agents within 75 miles are coming in to pick it up.

Q When he goes into the Calgary warehouse, to that particular agent it is 11.6?

A It is not a sale, it is an inter-station transfer to him.

Q You do not consider it a sale?

A It is an inter-station transfer

Q You then have a condition where your company establishes to its own agent at Airdrie a price of 11.6 f.o.b. your refinery or warehouse, Calgary and what, you can tell us no doubt, does that mean to the other companies, do they then ignore

your price of 11.6 or do they meet it when it comes to delivering to their dealers and agents?

A Well I presume it is optional with them whether they meet it or not but our information is, as we will indicate later, that we have been attempting to meet prices but not to beat them and we have plenty of invoices to support our stand on that. I want to say at this time, Mr. Plotkins, that we have no desire in Alberta to put in an allowance to sell below your prices or the price of any other local man and if we are doing so they will be withdrawn but we are pretty sure of our information that at the present time, that any allowances we put in last year or this year, have been made to meet prices already in effect that were lower than ours and at the present time do you know that our allowances were higher than the prices of any one of the local oil companies.

Q Now Mr. Halverson, I think you are quite sincere in what you say but I would like to analyse it with you and show you why I think your information only applies to your system of marketing and it is not true of the other companies. Now when you say that the price that the other companies sell at is lower than yours, do you mean is lower at Calgary or is lower at the point of consumption?

A Well it is lower at Calgary to start with and incidentally we have invoices to show it is lower at the point of consumption.

Q Yes?

A There has been a system of distribution grown up in the last twelve months in particular where the farmer who has a truck is being appointed a dealer and that farmer is getting 2 cents off the market, not only on White Gasoline but on other brands

as well and as far as we are concerned the only discount outside of our official allowance which we give is 1 cent to undivided dealers; when a trucker comes into our Calgary refinery he pays the posted tank waggon price. If a dealer comes in there and very few of them do, the maximum discounts they get, outside of the official allowance, is 1 cent but the competition with which we are competing gives 2 cents or a cent and a half a gallon to any farmer who has a truck more or less, to any trucker who comes in and that is the price with which we are competing.

Q Mr. Halverson, I am not going to analyse just what you have just said but I would like to bring out for the benefit of the Commission one principle which I think seems to be the trouble in your company, when you sell a farmer, a consumer now, I will take one point which I think is typical of that principle, in the Olds district, your price is based on Calgary plus freight, I mean your tank waggon?

A Our normal price structure is.

Q Yes?

A Yes.

Q Now your agent then is called upon to sell at that price and to deliver the gasoline to the farmer in the Olds district at that price?

A That is right.

Q Now then the difficulty as I see it, and I want you to make your comments on it, because this is the principle that I think we are both troubled with, the difficulty is that your price is based on freight which is considerably higher than the actual cost to your competitors of laying down that product at Olds or to the farmer at Olds by truck and therefore while we both sell at one price f.o.b. Calgary, your

company and our company we will say for instance, our dealer who happens to take the goods by truck from our refinery or bulk station, when he lands it to the farmer in Olds in competition with your dealer or agent landing it to the farmer, our dealer has a considerable advantage in that his trucking costs, even allowing for a fair profit, brings his cost, as compared with your agent's cost, down considerably. Now is that not the big trouble?

A That is not entirely the whole trouble because we have invoices to show that products are being sold at destination at less than our prices.

Q Yes?

A You are referring to Ex Calgary. It is quite obvious of course that a dealer who comes into Calgary or a farmer, with his own truck, he does not pay really any transportation at all except the gas and oil which he uses. He is coming into Calgary perhaps to do some shopping or something and we cannot carry on a distribution system, to give service 12 months a year, based on that kind of transportation.

Q I am not referring to that kind of transportation, Mr. Halverson, I am asking you to take into consideration the legitimate dealer that comes into Calgary and buys his gasoline for cash in his own drums at the same price from us as he does, as he would from your company as far as tank waggon is concerned and he receives the same agent's discount, now that man is not an unfair competition, I mean he has to consider costs of his trucking and distribution, now that particular man when he reaches, when he delivers the goods in the Olds District to a farmer, can do it at considerably less cost than what you allow yours based on freight rates plus cost of distributing back onto the farmer, and that is the trouble between us, in other

words your company at the present time has not seen fit as yet to eliminate, in certain territories, the freight rate and face actualities or realities in the form of lower costs in transportation, is that not the trouble?

(Go to number 9387)

A Not quite.

Q Well, what is it?

A The posted tank waggon price is 14 cents.

Q Yes?

A In case that form of transportation enjoys all the advantages which you say it does, the local oil company would not, I cannot see any reason why they should voluntarily reduce their price to 11½ cents and 11 and 10½ cents because if they had sold at 14 cents, according to your line of reasoning, they would have had an advantage over us on account of lower transportation and I am a little backward to understand why, if that was the case, it was necessary to quote prices at Calgary here of 11½ and 11 and 10½ cents.

Q Mr. Halverson, what is the spread between Calgary and Olds, Mr. Stevens can tell us now.

MR. FRAWLEY: 16.5 and 18.2.

MR. STEVENS: 1.7.

WITNESS: The freight to Olds is 1.68 cents per gallon, 21 cents a hundred.

Q MR. PLOTKINS: Have you any idea what you would calculate the freighting by truck?

A No.

Q Or what your Company pays on an average per mile of 1000 gallons?

A No.

Q Now we will take Olds, your differential based on actual freight rate is 1.7 per gallon, that is what Mr. Stevens tells me, and that only lays it down in Olds to your agents, it does not lay it down on the farm?

A No.

Q Your agent is still called upon to take and rehandle that into drums and take it out to the farmer at his own expense, out of the commission which you allow him, that is right is it not?

A Yes.

Q Now, if the same agent were to come into your Company and did not have a bulk station or had only a warehouse and were allowed to take that drum of gasoline out of your warehouse or refinery and calculate the competitive trucking rate, in other words, what somebody else would deliver that drum of gasoline down to the farmer in the Olds district, we find that based on 15 cents a mile a thousand, which is higher than the prevailing trucking rate, that is the rate we calculate on, although competition is even less than that, that he could lay it down on the farm for 9-10ths of a cent a gallon instead of 1.7, plus rehandling and the additional cost of delivering, what have you to say to that?

A Well, if we were a local oil company pursuing a policy of expediency, with no responsibility towards the Province of Alberta, under present conditions there might be some way of closing down our stations within 100 miles of Calgary and telling everybody to come to Calgary and get their stuff.

Q No --

A I mean that is, I am talking common sense at the moment. it is either a case of doing that or keeping our system of distribution going. We have agents at Olds, we have agents at all these points who are very necessary when the road conditions are bad and the harvest season is on

and we have to see to it that they maintain a reasonable share of the market. Now, we do know there is the odd farmer, and many of them, who has an extra truck, maybe the father runs the farm and the son becomes a trucker and he comes into Calgary and he buys a few barrels of oil and he sells them to a few farmers in his own neighborhood and what is more he gets the dealer's price, and I understand he is getting a dealer's license and a wholesaler's license from the Government. Well if there are enough of those farmers that become wholesalers using their trucks in their spare time, the thing which we are faced with within 100 miles of Calgary is whether we are going to give over that system of distribution, because the agents cannot carry on at Olds if every farmer when it pleases him, is to be a wholesaler hauling from Calgary and then when the peak season comes on, we are supposed to be there to take care of him, it doesn't work but in the meantime we have to protect our gallonage.

Q Does it involve all that, does it involve anything except the method of transporting gasoline by rail, I mean after all the only difference is shipping by truck instead of by rail, it doesn't involve scrapping your present distribution system?

A We move it today, Mr. Plotkins, by truck up to maybe 100 miles but the only difference of opinion may be this, that instead of trying to drive a hard bargain with our agents, we are giving them the tank car rate but on products for which we do not have bulk storage they are moving that for us at tank car rates as well and we are substantially cutting down on the inter-station transfer. I am told

that chartered truckers can be secured for around 10% less than railway rates. Probably somebody can drive a harder bargain but I do know that people who move substantial quantities are willing to pay chartered truckers 10% below tank car rates, which is not a very big margin.

Q Well that may be perfectly true when you come to long distances, as I understand it, the information I have and in discussing it with your Alberta Sales Manager, is that your Company does use trucks to bring products to Edmonton for instance, and pay on the basis of freight rates less 10% or something to that effect but when we come to points that are closer to Calgary, where all your competition seems to be, because that seems to be the district where you have reduced prices to meet that competition, is it not the fact then that all that is necessary for your company to do, to eliminate that which you call unfair competition, is to face the realities of the situation and base your differentials, not on carload freight rates but on the cost of profitably transporting that oil today with present means, to those points?

A I do not mean to infer in the first place it is unfair competition. It is a new type of competition and so far as moving our products by trucks we are naturally anxious to reduce our own marketing expenses and to that extent there is no difference in our viewpoint, that is if trucking is cheaper than moving it by railway, we want to truck but the difference in viewpoint may be that we must look to high pressure people who are moving products for rates less than a living rate.

Q Well, let us examine that, Mr. Halverson. When I said 9/10's of a cent a gallon between here and Calgary, that was based on 15¢ per mile per thousand gallons.

MR. FRAWLEY: You said between here and Calgary.

MR. PLOTKINS: Between here and Okotoks, or between here and any other point. 15¢ a thousand a mile. For instance, if he hauls it 60 miles it would make 120 miles return and work out to 17½ miles at a cost of 9/10's of a cent a gallon. Now, your company has investigated the cost of trucking, no doubt, have they?

A Not very extensively. We do not feel at the present time warranted in making a big capital investment in new trucks. As I pointed out in the brief, the railways have lost such a tremendous amount of traffic that it seems to me their self interest is going to dictate to them a drastic revision downward in freight rates. I have no idea what their plans are but from the standpoint of common sense it looks to me as though that is a contingency we might expect. In the meantime, of course, trucking up to 100 miles at least is the cheapest mode of transportation, of transporting. But in the meantime we do not like to go ahead and buy 50 or 100 trucks at a tremendous capital expense. We have two ways of trucking in the meantime. We have first our agent trucking and the other is the jobber trucking. The jobber trucking, I believe, we can get for about 10% below the railway rate. Perhaps we could drive a harder bargain. I know one company has attempted to get its transport cost down and the best they can do is to get 10% off the tank car rate, regardless of distance. The other is to let our agents do the trucking.

Q I am asking you, Mr. Halverson, if you would take 15¢ a mile a thousand as a basis. Now, the reason I am taking that figure is that we operate a large fleet of trucks and on that figure we make a considerable profit. In other words, we make more than a normal profit. We can truck profitably up to 300 miles on that basis. Now, that would take in most of your territory in Alberta from the Calgary refinery. Now, I have taken that up with your company several times and I would like you to give your opinion a little more definitely than you have so far as to why the differentials that exist between the Calgary refinery and all the country points in Alberta should not be based on the cheapest method of transportation instead of the highest cost transportation. Because it is true what you say, that you do not feel that your company would be justified in going ahead and buying a lot of trucks, of course, because conditions may change and the freight rates may come down. I quite appreciate your point. But there are trucks available offering themselves to you. Your own agents have trucks and surely you have made a study. You know what the costs are because your own company has a large fleet of trucks all over Canada. So that you must know within a pretty close range what it would cost your company or what it would cost anybody to profitably truck per mile per thousand gallons, or per gallon. So that with this competition that has been facing you for several years since roads have improved and since trucks have become a competitive factor, why do you persist in an endeavour to prevent the other man from taking advantage of more modern methods of transportation and better roads, instead of meeting competition

by giving the public a low price that will transform the realities of improved transportation methods into savings per gallon or a price per gallon?

A Of course, we are not at all concerned about your method of transportation. What we are concerned about is reducing our own costs. I think it can be taken for granted that the company which I represent is very interested in making a little profit and reducing expense. They are not deliberately throwing money away to the railway for any charitable reasons. We feel beyond a certain limited district of 100 miles from Calgary that rail is and will be the most economical method of distribution for us, keeping in mind that we are not an in-and-out company that gives service when the roads are good. We have to be there twelve months of the year, peak seasons as well as off seasons. And we definitely feel beyond 100 miles radius that our system of distribution, if we are to be permanent marketers, is the most economical one for us and that is why we are staying with it. Up to 100 miles it is a different problem. But the situation that confronts us to-day may be temporary and we do not like to jump too fast. We do not like to get stampeded. It is possible that if the present rail structures continue as they are it may be necessary for us to zone our prices.

MR. FRAWLEY: Again back to that.

A Zone our prices within say 100 miles of Calgary, based, as Mr. Plotkins suggests, on the lower mode of transportation. But that lower mode of transportation in our opinion does not generally apply beyond the 100 miles limit.

Q Mr. Halverson, British American has been compelled - I will use the word - to recognize that situation and they have

changed their method of distribution.

A Well, I dealt with that in my brief this morning. It is our considered opinion that the most economical method of distribution is moving your product direct to destination, and I gave some figures this morning in the brief on that.

Q You mean in general?

A Yes. To ship to a place like Camrose and re-truck from there is not as economical as moving your product direct to Tofield. For instance, the difference in the railway rate between Wetaskiwin and Millet is .08¢, less than a tenth of a cent per gallon. If we were to use say Wetaskiwin as the central point we would have to truck it across to Millet for a tenth of a cent, less than a tenth of a cent per gallon, and it would add to our cost.

Q If you used trucks instead of tank cars would not that difficulty disappear?

A Up to a certain distance.

Q You would not have to re-ship?

A Up to a certain distance.

Q Within the distance your company has felt it is profitable to truck direct?

A Yes.

Q MR. FRAWLEY: Just one question, it is a bit spotty and I want to ask this one question. If I regard the spreads as the result of these seven new differentials. Take Irracana, for instance. I suppose they are all the same. You took the point where the tank waggon is the same. These seven points with the tank waggon originally was the same. Take Irracana and see what you have done. You now have an effective price to the A. B. A. dealer of

11.6 cents. Now, in order to explain for the record the A. B. A. dealer, you keep using the expression "undivided dealer", that is the same thing.

THE CHAIRMAN: What do you mean by A. P. A.?

MR. FRAWLEY: A. B. A. He is now called "undivided". We will withdraw the A. B. A. expression.

A Authorized Buyer's Agreement.

Q 100% dealer is the better term.

Q THE CHAIRMAN: You mean he is an individual who buys nothing else or who will not sell anyone else's products but sells the products of the Imperial?

MR. FRAWLEY: That is what it is.

THE CHAIRMAN: That is undivided?

MR. FRAWLEY: He is an undivided dealer.

A What was it you wanted to know?

Q If you would use that Exhibit "257" I think. Acto gasoline. Acto gasoline to the undivided dealer at Irracana now is a price of 11.6 cents?

A That is right.

Q He has a price on 3 Star of 16.6?

A No, the posted tank waggon price on 3 Star there is 17.6, with 1¢ off to the undivided dealer.

Q 16.6?

A That is right.

Q That is what I said. It is a price of 11.6 on Acto and 16.6 on 3 Star and 19.1 on Esso?

A Yes, that is right.

Q What you have done, you have used a spread of 4 cents between the 3rd structure and the 2nd structure, and a 2½¢ spread between the two brands of leaded products remains the same?

A That is right.

Q That is out of line, of course, is it not, these spreads, is it not pretty hard to justify a 4 cent spread between Acto and 3 Star?

A For a number of years our spread used to be 5 cents but as the successive reductions in the 3 Star we cut it down to $2\frac{1}{2}$ cents. At the same time, as I mentioned in my brief, if we are to operate we have to look at the over-all picture and at the same time our prices must be flexible enough to meet conditions.

Q Yes, but you have all over Alberta now a pretty constant spread between the 3rd and 2nd. What is it? What is it in Edmonton, for instance?

A You mean Acto?

Q Between 3rd and 2nd?

A $2\frac{1}{2}$ cents. But in the low cost marketing area adjacent to Calgary it is more.

Q I know. It is now 4 cents. That is what I am pointing out to you. It is now 4 cents in this area. You do not expect to be able to get away from that very soon, do you?

A As I mentioned a moment ago, unless there is some readjustment in transport rates, we may have to zone prices around Calgary on the basis of lower costs, such as Mr. Plotkins suggested.

Q Just one more thing. You said you were faced with this situation within 100 miles of Calgary; that you regarded truck transportation as being pretty stiff competition as against your system of using the railway within 100 miles?

A Yes.

Q I do not quite understand why you only selected those seven points. Why not go the whole distance up to Red Deer with

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these differentials?

A I explained that a while ago. We had our choice of either putting in a wholesale outlet on the east road, the west road and the south road the same as the others were doing here, and scrapping these agencies that we have around Calgary, or putting these agents in a position to compete. Instead of putting in further duplication of distribution, which we considered is temporary and unnecessary, we thought the right thing to do was to use these agents.

Q It was not then, I think I understand, it was not then to meet the effect of truck competition within 100 miles of Calgary?

A No. It was in a way to put us in a position to compete for the business of these farmers and truckers, especially the farmers.

Q That would pass on the south road, the north road and on the east road but not on the west road and that is why the west road was not used?

A Or if they want to buy our products they can buy them there without going to the refinery. When they come to Calgary they buy down town, they won't go to the refinery.

Q MR. PLOTKINS: Just one question. Do you lose all this gallonage, or some of it might go to your jobbers. In other words, these farmers that come into Calgary and buy at a lower price, might not some of that gallonage go back to you just the same?

A It might conceivably, but my information, Mr. Plotkins, is that most of it is being picked up from organizations like the Lion Oils, Outen Bros., Mayland, Becker, Economy Oils and Great West Distributors. Very little of it

[illegible]

[illegible] which we considered is the [illegible]

thought the same thing [illegible]

[illegible]

[illegible] of these [illegible]

[illegible]

Or if they want to buy our products they can buy them at [illegible]

within 6 months [illegible]

[illegible]

from the North Star or the Canadian that are buying from us. Most of that gallonage, I do not think, originates at our refinery. Some of it does, but very little.

Q I may inform you at this time we have absolutely no farm business. We are in the same position you are. We have lost it all. So it is not our company that is getting it.

THE CHAIRMAN: Anything more, Mr. Frawley?

MR. FRAWLEY: No, that is all, thanks.

(At this stage the Hearing was adjourned until 10:30 A. M. 20th June, 1939.)

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